

Fiscal Year

# 2006 Performance and Accountability Report



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# Table of Contents

PART 1: MANAGEMENT DISCUSSION & ANALYSIS . . . . .	1
Mission, Vision, Values, & Organization . . . . .	3
NASA's Mission Is on Track . . . . .	3
Making Progress . . . . .	3
NASA's Values . . . . .	4
NASA's Organization . . . . .	4
NASA Headquarters . . . . .	4
Building Healthy NASA Centers . . . . .	5
Measuring NASA's Performance . . . . .	7
Establishing Government Performance and Results Act (GPRA) Performance Measures . . . . .	7
Rating NASA's Performance . . . . .	7
Program Assessment Rating Tool (PART) . . . . .	12
President's Management Agenda (PMA) . . . . .	12
Major Program Annual Reports . . . . .	13
Performance Overview . . . . .	15
Progress Toward Achieving NASA's Strategic Goals . . . . .	15
A Guide to Performance Overviews . . . . .	15
Strategic Goal 1: Fly the Shuttle as safely as possible until its retirement, not later than 2010. . . . .	16
Strategic Goal 2: Complete the International Space Station in a manner consistent with NASA's International Partner commitments and the needs of human exploration. . . . .	18
Goal 3: Develop a balanced overall program of science, exploration, and aeronautics consistent with the redirection of the human spaceflight program to focus on exploration. . . . .	20
Sub-goal 3A: Study Earth from space to advance scientific understanding and meet societal needs. . . . .	22
Sub-goal 3B: Understand the Sun and its effects on Earth and the solar system. . . . .	25
Sub-goal 3C: Advance scientific knowledge of the origin and history of the solar system, the potential for life elsewhere, and the hazards and resources present as humans explore space. . . . .	28
Sub-goal 3D: Discover the origin, structure, evolution, and destiny of the universe, and search for Earth-like planets. . . . .	31

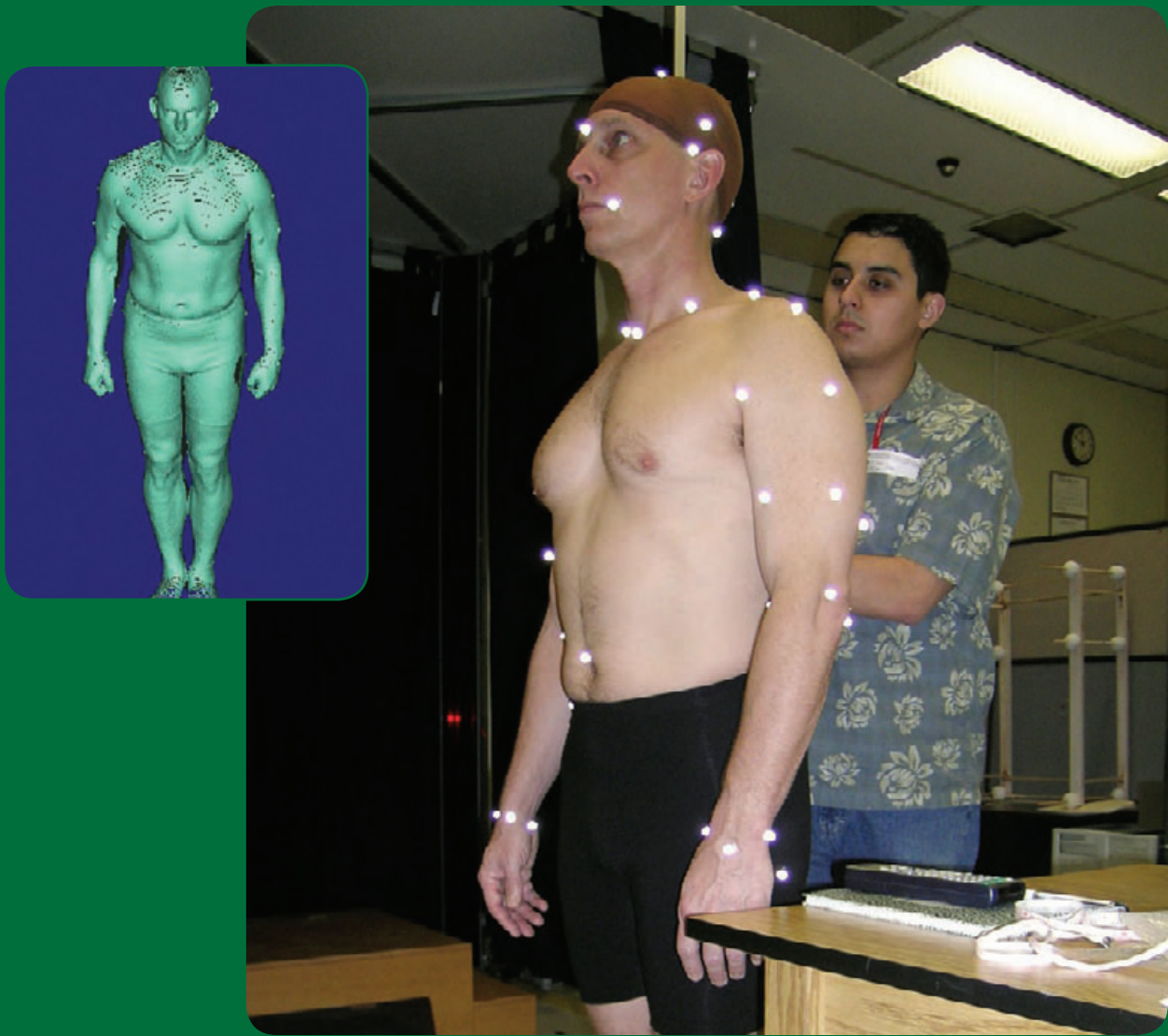
Sub-goal 3E: Advance knowledge in the fundamental disciplines of aeronautics, and develop technologies for safer aircraft and higher capacity airspace systems. . . . .	34
Sub-goal 3F: Understand the effects of the space environment on human performance, and test new technologies and countermeasures for long-duration human space exploration. . . . .	37
Strategic Goal 4: Bring a new Crew Exploration Vehicle into service as soon as possible after Shuttle retirement. . . . .	40
Strategic Goal 5: Encourage the pursuit of appropriate partnerships with the emerging commercial space sector. . . . .	43
Strategic Goal 6: Establish a lunar return program having the maximum possible utility for later missions to Mars and other destinations. . . . .	46
<b>Financial Overview . . . . .</b>	<b>49</b>
Financial Statements and Stewardship . . . . .	49
Overview of Financial Position . . . . .	50
Assets . . . . .	50
Liabilities . . . . .	51
Ending Net Position . . . . .	52
Results of Operations . . . . .	52
Limitation of the Financial Statements . . . . .	53
Key Financial-Related Measures . . . . .	53
<b>Systems, Controls, &amp; Legal Compliance . . . . .</b>	<b>55</b>
Overview . . . . .	55
Management Assurances . . . . .	57
Corrective Action Plan. . . . .	58
New Material Weakness. . . . .	58
Continuing Material Weaknesses . . . . .	58
Closed Items . . . . .	59
Office of the Inspector General Statement on Material Weaknesses at the Agency . . . . .	61
Federal Financial Management Improvement Act . . . . .	70
Improper Payments Information Act . . . . .	70
NASA's Efforts to Identify Erroneous/Improper Payments . . . . .	70
NASA's Planned Fiscal Year 2007 IPIA Compliance Approach . . . . .	71
Legal Compliance . . . . .	72
<b>Looking Ahead . . . . .</b>	<b>73</b>
Staying on Target and on Budget . . . . .	73
Transitions. . . . .	73
Maximizing NASA's Workforce . . . . .	73
Improving Agency Management . . . . .	74
Thinking (and Contracting) Outside of the Box. . . . .	75
Strengthening International Relationships and Collaboration . . . . .	75

PART 2: DETAILED PERFORMANCE DATA.....	77
Detailed Performance Data.....	79
NASA's Performance Rating System.....	79
Strategic Goal 1.....	82
Strategic Goal 2.....	85
Strategic Goal 3.....	88
Sub-goal 3A.....	89
Sub-goal 3B.....	99
Sub-goal 3C.....	104
Sub-goal 3D.....	110
Sub-goal 3E.....	117
Sub-goal 3F.....	122
Strategic Goal 4.....	126
Strategic Goal 5.....	130
Strategic Goal 6.....	132
Cross-Agency Support Programs.....	137
Education.....	137
Advanced Business Systems (Integrated Enterprise Management Program).....	138
Innovative Partnerships Program.....	139
Efficiency Measures.....	141
NASA's FY 2006 Performance Improvement Plan.....	143
PART 3: FINANCIALS.....	155
Message from the Chief Financial Officer.....	157
Financial Management Improvement.....	158
2006 Financial Management Improvement Efforts.....	158
Introduction to the Principal Financial Statements.....	160
Office of Inspector General Letter on Audit of NASA's Financial Statements.....	206
Report of the Independent Auditors.....	208
Chief Financial Officer's Response to the Audit Report of the Independent Auditors.....	235
APPENDICES.....	237
Appendix A: Audit Follow-up Actions.....	A-1
Appendix B: FY 2005 Performance Improvement Plan Follow-up.....	B-1
Appendix C: OMB Program Assessment Rating Tool (PART) Recommendations.....	C-1
Appendix D: Source Information.....	D-1





## Part 3: Financials



Previous page: A trainer helps lower astronauts Joseph Tanner and Heidemarie Stefanyshyn-Piper (partially obscured), both STS-115 mission specialists, into the water of NASA's Neutral Buoyancy Laboratory, located near the Johnson Space Center. Tanner and Stefanyshyn-Piper are attired in training versions of the Extravehicular Mobility Unit spacesuit. SCUBA-equipped divers are in the water to assist the crewmembers in their rehearsal, intended to help prepare them for work on the exterior of the International Space Station. (NASA)

Above: Astronaut Clayton Anderson, wearing shorts and a skull cap, remains still during a three-hour process in which NASA technicians use new laser technology to gather data about his physical measurements (large photo). The technicians run use the data to create a three-dimensional Audio Video Interleaved file of the astronaut's body (upper left) that they can use to match the astronaut with a spacesuit of the correct size and shape. By expanding and analyzing the database, scientists and engineers can determine what kinds of general body shapes, heights, arm lengths, hand sizes, and and other measurements are most common among those selected to fly in space. (NASA)



# Message from the Chief Financial Officer



NASA's financial community enters fiscal year (FY) 2007 with an unwavering commitment to achieving financial management excellence. Recognizing the progress we have made over the past year, we acknowledge continued room for improvement and fully accept responsibility for improving the health and operation of the Agency's financial management processes.

In FY 2006, the Agency implemented a broad program of corrective actions to address its financial management weaknesses. Progress on those corrective actions is the result of significant cross-Agency effort. Much of the work that remains is in the stabilization of improved processes so that they consistently and regularly deliver expected results. In their report, the Agency's independent auditors acknowledged the progress made in NASA's financial management processes, particularly in the areas of differences in Fund Balance with Treasury and the estimation of Unfunded Environmental Liabilities.

I am pleased to report that both of these weaknesses were resolved in FY 2006. NASA will continue to monitor reconciliation processes and other associated controls to ensure that these accounts remain firmly in control.



While the Agency has made progress, significant challenges remain. The Agency's independent auditors, have noted two modified repeat conditions, both material weaknesses, for FY 2006: Financial Systems, Analyses and Oversight; and Property, Plant and Equipment. System and process limitations continue to require compensating controls, and have limited NASA's ability to accumulate, analyze, and distribute reliable financial information. The Agency recognizes these deficiencies and continues to work diligently toward their resolution. We invite you to read the expanded financial management section that follows to learn more about these weaknesses and the improvement actions we completed in FY 2006.

In addition to the corrective actions taken, FY 2006 was also a year of preparation for a major update to NASA's Core Financial system. Enhancements to the system, to be implemented with the beginning of FY 2007, will further integrate our process changes and improve our systems. Also, we will continue to use the practice initiated last year to develop a FY 2006 Financial Audit Corrective Action Plan. We are working diligently to meet the requirements for an opinion to be rendered on our FY 2007 financial statements.

NASA's mission success includes healthy financial management and effective reporting on the resources entrusted to the Agency. We remain dedicated to achieving that mission.

Sincerely,

A handwritten signature in black ink that reads "Gwendolyn Sykes".

Gwendolyn Sykes  
Chief Financial Officer

## Financial Management Improvement

In FY 2006, NASA implemented a Financial Audit Corrective Action Plan (CAP) to address weaknesses identified in the 2005 financial audit. The steps the Agency took in support of the CAP leveraged the stabilization gains made in 2005. As of the 3rd Quarter of FY 2006, the Office of Management and Budget (OMB) acknowledged NASA's progress toward improved financial management by upgrading its measure for NASA's Financial Management PMA progress to "Yellow."

The Agency recognizes that there is much work to be done as it continues to improve NASA's financial management performance. NASA is aggressively working toward eliminating all financial weaknesses as a part of the Agency's effort toward achieving auditable financial records and actionable financial information for decision making. A summary of progress and accomplishments, by FY 2005 audit weakness, follows.

### 2006 Financial Management Improvement Efforts

#### 1. *Financial Systems, Analyses, and Oversight*

To improve NASA's ability to accumulate, analyze and distribute reliable financial information, the Agency has developed and is implementing procedures to validate financial data and processes in the Agency's Core Financial system, strengthened internal controls to ensure consistency with authoritative guidance, and aligned its external financial reporting with federal requirements.

Following NASA's Financial Management Requirements, Volume 19—Periodic Monitoring Controls Activities, each NASA Center conducts regular reconciliations of key financial accounts or activities. The results of these reconciliations, including associated corrective action plans, are certified by Center CFOs and reported to NASA Headquarters on a monthly basis. As a result, NASA is given a view of any emerging systemic data integrity issues, which facilitates coordinated improvements designed to eliminate the root causes of issues.

#### **Statement of Material Weakness:**

Financial Systems, Analyses, and Oversight

#### **Summary Auditor Finding:**

"Although progress was made [since the 2004 audit], significant financial management issues continue to impair NASA's ability to accumulate, analyze, and distribute reliable financial information."

(Reference: NASA FY 2005 Performance and Accountability Report (PAR), Part 3, page 193)

In addition, the Agency prepares monthly and quarterly Agency financial statements within 30 days of period close. This process includes the documentation of any data anomalies or corrections, and statement analyses. Monthly financial statements are used to ensure appropriate processing of financial information. Also, compared to FY 2005, NASA modified the presentation of its Statement of Net Costs to provide a breakdown of net costs by major lines of business, consistent with Office of Management and Budget Circular A-136. The ability to associate costs to major lines of business is a result of a major account structure change that NASA introduced at the beginning of the fiscal year.

Finally, the Agency developed and published monthly financial metrics, providing both process and outcome measures of NASA's financial performance. These metrics are reviewed at monthly financial management senior leadership meetings to discuss performance and trends, and to share best practices.

Throughout 2007, the Agency will continue to review and certify Center-level financial accounts and activities on a monthly basis. Financial statements and metrics, also on a monthly basis, will be prepared and reviewed by management.

#### 2. *Property, Plant and Equipment*

To address material weaknesses in Property, Plant and Equipment accounting, NASA has taken steps in FY 2006 to rectify policy and process weaknesses.

NASA is considering a change in its accounting policy for Theme Assets to reclassify some costs previously categorized as General Property, Plant & Equipment (PP&E) as Research and Development (R&D) expenses. In



FY 2006, NASA drafted a policy to implement this change and requested that FASAB clarify the accounting standards the Agency used as the basis for the draft change. NASA anticipates a response from FASAB in FY 2007.

Also in 2006, NASA implemented compensating controls to address PP&E process weaknesses, including establishment of procurement guidance to facilitate improved accounting for property furnished to contractors. NASA is developing improved business processes for all asset categories to improve the effective lifecycle management of PP&E.

In 2007, the Agency expects to finalize its accounting treatment policy for NASA's Theme Assets. Also, NASA will align policies, processes and systems for all of its asset categories with the appropriate accounting treatments. This includes alignment of contract requirements, related primarily to contractor property reporting, with agreed upon policies.

### 3. *Fund Balance with Treasury*

To address NASA's 2005 material weakness in Fund Balance with Treasury (FBWT), the Agency has resolved outstanding reconciling items from prior periods and introduced reconciliation procedures that are tracking current period differences so they may be resolved in a timely manner. NASA Centers are required to provide monthly reconciliation reports for Agency measurement and oversight.

NASA will continue to monitor FBWT differences on a monthly basis. Corrective actions will be taken on each difference, and progress on those actions will be monitored to ensure that differences are resolved in a timely manner.

### 4. *Estimation of Environmental Liabilities*

To address weaknesses in the estimation of NASA's unfunded environmental liabilities (UEL), the Agency implemented policies, processes, tools and training that generated auditable estimates of UEL for all Centers by the second Quarter of FY 2006.

To develop these estimates, NASA enhanced the policies and procedures for the estimation of unfunded environmental liabilities for both environmental engineers and accountants. These policies and procedures are documented and consistent for all Centers, resulting in more uniform, reliable and valid estimates.

The Agency also held joint training classes for environmental engineers and accountants responsible for determining and documenting unfunded environmental liability (UEL) to ensure consistent understanding and practice.

#### **Statement of Material Weakness:**

Enhancements needed for controls over Property, Plant and Equipment (PP&E) and materials

#### **Summary Auditor Finding:**

"Consistent with prior year audit reports, our review of property, plant, and equipment (PP&E), totaling approximately \$35.0 billion, identified serious weaknesses in internal control that, if not corrected, could prevent material misstatements from being detected and corrected in a timely manner."

(Reference: NASA FY 2005 Performance and Accountability Report (PAR), Part 3, page 203)

#### **Statement of Material Weakness:**

Further Research Required to Resolve Fund Balance With Treasury Differences

#### **Summary Auditor Finding:**

"Although we were informed that many errors from FY 2003 were resolved, significant errors within the accounting system were still being identified by NASA in FY 2005. Fund balance with Treasury reconciliation processes were ineffective in FY 2004 and much of FY 2005, through the date of our visits to centers, but it is our understanding that steps taken by NASA in the last quarter of the year are believed by NASA management to have substantially improved the effectiveness of such reconciliations."

(Reference: NASA FY 2005 Performance and Accountability Report (PAR), Part 3, page 201)

#### **Statement of Reportable Condition:**

Internal controls in estimating NASA's Environmental Liabilities require enhancement

#### **Summary Auditor Finding**

"During our review of NASA's environmental liability estimates totaling \$825 million as of September 30, 2005, and related disclosures to the financial statements, we continued to note weaknesses in NASA's ability to generate an auditable estimate of its unfunded environmental liabilities (UEL) and to identify potential financial statement disclosure items because of a lack of sufficient, auditable evidence."

(Reference: NASA FY 2005 Performance and Accountability Report (PAR), Part 3, page 207)

## Introduction to the Principal Financial Statements

The Principal Financial Statements have been prepared to report the financial position and results of operations of the National Aeronautics and Space Administration (NASA). The Statements have been prepared from the books and records of NASA in accordance with formats prescribed by the Office of Management and Budget (OMB) in Circular A-136, Financial Reporting Requirements. The statements are in addition to financial reports prepared by the Agency in accordance with OMB and U.S. Department of the Treasury (Treasury) directives to monitor and control the status and use of budgetary resources, which are prepared from the same books and records. The statements should be read with the understanding that they are for a components of the U.S. Government, a sovereign entity. The Agency has no authority to pay liabilities not covered by budgetary resources. Liquidation of such liabilities requires enactment of an appropriation. Comparative data for 2005 are included where available.

NASA's Principal Financial Statements include the following:

The **Consolidated Balance Sheet** provides information on assets, liabilities, and net position similar to balance sheets reported in the private sector. Assets must equal the sum of liabilities and net position.

The **Consolidated Statement of Net Cost** reports the components of the net costs of the Agency's operations for the period. The net cost of operations consists of the gross cost incurred by the Agency less any exchange (i.e., earned) revenue from activities.

The **Consolidated Statement of Changes in Net Position** reports the beginning net position, the transactions that affect net position for the period, and the ending net position.

The **Combined Statement of Budgetary Resources** provides information on how budgetary resources were made available and their status at the end of the year. Information in this statement is reported on the budgetary basis of accounting.

The **Consolidated Statement of Financing** reports the relationship between budgetary transactions and financial transactions.

**Required Supplementary Stewardship Information** provides information on the Agency's Research and Development costs.

**Required Supplementary Information** contains a Combined Statement of Budgetary Resources and information on Deferred Maintenance.

**National Aeronautics and Space Administration**  
**Consolidated Balance Sheet**  
**As of September 30, 2006, and September 30, 2005**  
(In Millions)

	Unaudited 2006	Unaudited 2005
<b>Assets (Note 2):</b>		
Intragovernmental Assets		
Fund Balance with Treasury (Note 3)	\$ 9,585	\$ 8,146
Investments (Note 4)	17	17
Accounts Receivable, Net (Note 5)	180	136
Total Intragovernmental Assets	9,782	8,299
Accounts Receivable, Net (Note 5)	5	60
Inventory and Related Property, Net (Note 6)	2,330	3,019
General Property, Plant and Equipment, Net (Note 7)	33,193	34,926
<b>Total Assets</b>	<b>\$ 45,310</b>	<b>\$ 46,304</b>
 <b>Stewardship PP&amp;E (Note 17)</b>		
 <b>Liabilities (Note 8):</b>		
Intragovernmental Liabilities		
Accounts Payable	\$ 145	\$ 56
Other Liabilities (Note 9)	157	124
Total Intragovernmental Liabilities	302	180
Accounts Payable	1,703	2,076
Federal Employee and Veteran Benefits	60	62
Environmental and Disposal Liabilities (Note 10)	893	825
Other Liabilities (Notes 9 and 11)	355	340
<b>Total Liabilities</b>	<b>3,313</b>	<b>3,483</b>
 <b>Net Position:</b>		
Unexpended Appropriations	6,981	5,318
Cumulative Results of Operations	35,016	37,503
<b>Total Net Position</b>	<b>41,997</b>	<b>42,821</b>
<b>Total Liabilities and Net Position</b>	<b>\$ 45,310</b>	<b>\$ 46,304</b>

The accompanying notes are an integral part of this statement.



**National Aeronautics and Space Administration**  
**Consolidated Statement of Net Cost**  
**For the Fiscal Year Ended September 30, 2006**  
(In Millions)

**Cost by Business Line**

	Unaudited 2006
<b>Science</b>	
Gross Costs	\$ 6,628
Less: Earned Revenue	348
Net Costs	<u>6,280</u>
<b>Exploration Systems</b>	
Gross Costs	2,704
Less: Earned Revenue	88
Net Costs	<u>2,616</u>
<b>Aeronautics Research</b>	
Gross Costs	1,129
Less: Earned Revenue	79
Net Costs	<u>1,050</u>
<b>Space Operations</b>	
Gross Costs	8,120
Less: Earned Revenue	424
Net Costs	<u>7,696</u>
<b>Net Cost of Operations</b>	<u><u>\$ 17,642</u></u>

The accompanying notes are an integral part of this statement.

**National Aeronautics and Space Administration**  
**Consolidated Statement of Net Cost**  
**For the Fiscal Year Ended September 30, 2005**  
(In Millions)

	Unaudited 2005	
<b>Program Cost:</b>		
Gross Costs	\$	16,085
Less: Earned Revenues		879
<b>Net Cost of Operations</b>	<b>\$</b>	<b>15,206</b>

The accompanying notes are an integral part of this statement.

National Aeronautics and Space Administration  
Consolidated Statement of Changes in Net Position  
For the Fiscal Years Ended September 30, 2006, and September 30, 2005  
(In Millions)

	Unaudited 2006	Unaudited 2005
<b>Cumulative Results of Operations:</b>		
Beginning Balances	\$ 37,503	\$ 36,934
<b>Budgetary Financing Sources:</b>		
Appropriations Used	14,958	15,588
Nonexchange Revenue	48	35
<b>Other Financing Sources:</b>		
Transfers In Without Reimbursement	—	1
Imputed Financing	149	151
Total Financing Sources	15,155	15,775
Net Cost of Operations	(17,642)	(15,206)
Net Change	(2,487)	569
<b>Cumulative Results of Operations</b>	<b>\$ 35,016</b>	<b>\$ 37,503</b>
<b>Unexpended Appropriations:</b>		
Beginning Balances	\$ 5,318	\$ 4,771
<b>Budgetary Financing Sources:</b>		
Appropriations Received	16,842	16,324
Appropriations Used	(14,958)	(15,588)
Appropriations Transferred In/Out	26	—
Other Adjustments	(247)	(189)
Total Budgetary Financing Sources	\$ 1,663	\$ 547
Total Unexpended Appropriations	\$ 6,981	\$ 5,318
<b>Net Position</b>	<b>\$ 41,997</b>	<b>\$ 42,821</b>

The accompanying notes are an integral part of this statement.



**National Aeronautics and Space Administration**  
**Combined Statement of Budgetary Resources**  
**For the Fiscal Years Ended September 30, 2006, and September 30, 2005**  
(In Millions)

	Unaudited 2006	Unaudited 2005
<b><u>Budgetary Resources:</u></b>		
Unobligated Balance, Brought Forward, October 1:	\$ 2,241	\$ 3,101
Recoveries of Prior Year Unpaid Obligations	368	10
 Budgetary Authority		
Appropriation	16,843	16,315
Spending Authority from Offsetting Collections		
Earned		
Collected	989	851
Change in Receivables from Federal Sources	41	21
Change in Unfilled Customer Orders		
Advance Received	57	10
Without Advance from Federal Sources	(208)	117
Subtotal	<u>17,722</u>	<u>17,314</u>
 Nonexpenditure Transfers, Net		
Actual Transfers, Budget Authority	26	—
 Permanently Not Available		
Cancellations of Expired and No-year Accounts	(37)	(60)
Enacted Reductions	(210)	(129)
<b>Total Budgetary Resources</b>	<b><u>\$ 20,110</u></b>	<b><u>\$ 20,236</u></b>
 <b><u>Status of Budgetary Resources:</u></b>		
Obligations Incurred (Note 14)		
Direct	\$ 16,768	\$ 16,979
Reimbursable	1,005	1,019
Total Obligations Incurred	<u>17,773</u>	<u>17,998</u>
 Unobligated Balance		
Apportioned	2,143	2,073
Exempt from Apportionment	4	4
Total Unobligated Balances, Available	<u>2,147</u>	<u>2,077</u>
 Unobligated Balance Not Available	190	161
<b>Total Status of Budgetary Resources</b>	<b><u>\$ 20,110</u></b>	<b><u>\$ 20,236</u></b>

The accompanying notes are an integral part of this statement.

**National Aeronautics and Space Administration**  
**Combined Statement of Budgetary Resources (Continued)**  
**For the Fiscal Years Ended September 30, 2006, and September 30, 2005**  
(In Millions)

	Unaudited 2006	Unaudited 2005
<b><u>Change in Obligated Balance:</u></b>		
Obligated Balances, Net		
Unpaid Obligations Brought Forward, October 1 (Note 13)	\$ 6,525	\$ 4,972
Less: Uncollected Customer Payments from Federal Sources, Brought Forward, October 1	552	413
<b>Total Unpaid Obligated Balances, Net</b>	<b>5,973</b>	<b>4,559</b>
 Obligations Incurred, Net	 17,773	 17,998
Less: Gross Outlays	16,259	16,472
 Less: Recoveries of Prior Year Unpaid Obligations	 368	 10
Change in Uncollected Customer Payments from Federal Sources	167	(138)
 Obligated Balance, Net, End of Period		
Unpaid Obligations	7,671	6,488
Less: Uncollected Customer Payments from Federal Sources	385	551
<b>Total, Unpaid Obligated Balance, Net, End of Period</b>	<b>7,286</b>	<b>5,937</b>
 <b><u>Net Outlays:</u></b>		
Net Outlays:		
Gross Outlays	16,259	16,472
Less: Offsetting Collections	1,045	861
Less: Distributed Offsetting Receipts	8	—
<b>Net Outlays</b>	<b>\$ 15,206</b>	<b>\$ 15,611</b>

The accompanying notes are an integral part of this statement.

**National Aeronautics and Space Administration**  
**Consolidated Statement of Financing**  
**For the Fiscal Years Ended September 30, 2006, and September 30, 2005**  
(In Millions)

	Unaudited 2006	Unaudited 2005
<b><i>Resources Used to Finance Activities:</i></b>		
<b>Budgetary Resource Obligated</b>		
Obligations Incurred	\$ 17,773	\$ 17,998
Less: Spending Authority from Offsetting Collections and Recoveries	1,247	1,009
Obligations Net of Offsetting Collections and Recoveries	16,526	16,989
Less: Offsetting Receipts	8	—
<b>Net Obligations</b>	<b>16,518</b>	<b>16,989</b>
<b>Other Resources:</b>		
Transfers In Without Reimbursements	—	1
Imputed Financing from Costs Absorbed by Others	149	151
<b>Net Other Resources Used to Finance Activities</b>	<b>149</b>	<b>152</b>
<b>Total Resources Used to Finance Activities</b>	<b>16,667</b>	<b>17,141</b>
<b><i>Resources Used to Finance Items Not Part of the Net Cost of Operations</i></b>		
Change in Budgetary Resources Obligated for Goods, Services, and Benefits		
Ordered but Not Yet Provided	(1,598)	(1,389)
Resources That Fund Expenses Recognized in Prior Periods	(47)	(194)
Budgetary Offsetting Collections and Receipts that Do Not Affect the Net Costs of Operations—Other	55	(35)
Resources that Finance the Acquisition of Assets	(3,474)	(4,794)
Other Resources or Adjustments to Net Obligated Resources that Do Not Affect Net Cost of Operation	—	(1)
<b>Total Resources Used to Finance Items Not Part of the Net Cost of Operations</b>	<b>(5,064)</b>	<b>(6,413)</b>
<b>Total Resources Used to Finance the Net Cost of Operations</b>	<b>11,603</b>	<b>10,728</b>

The accompanying notes are an integral part of this statement.



National Aeronautics and Space Administration  
Consolidated Statement of Financing (Continued)  
For the Fiscal Years Ended September 30, 2006, and September 30, 2005  
(In Millions)

	Unaudited 2006	Unaudited 2005
<i>Components of Net Cost That Will Not Require or Generate Resources in the Current Period</i>		
<i>Components Requiring or Generating Resources in Future Periods: (Note 16)</i>		
Increases\Decreases in Annual Leave Liability	8	(4)
Increase in Environmental and Disposal Liability	68	—
Increase in Exchange Revenue Receivable from the Public	—	28
Other	180	44
<b>Total Components of Net Cost that Will Require or Generate Resources in Future Periods</b>	<b>256</b>	<b>68</b>
 <i>Components Not Requiring or Generating Resources</i>		
Depreciation	5,730	4,417
Revaluation of Assets or Liabilities	7	—
Other	46	(7)
<b>Total Components of Net Cost of Operations that Will Not Require or Generate Resources</b>	<b>5,783</b>	<b>4,410</b>
<b>Total Components of Net Cost of Operations that Will Not Require or Generate Resources in the Current Period</b>	<b>6,039</b>	<b>4,478</b>
 <b>Net Cost of Operations</b>	<b>\$ 17,642</b>	<b>\$ 15,206</b>

The accompanying notes are an integral part of this statement.

**National Aeronautics and Space Administration**  
**Notes to Financial Statements**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**

**NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Reporting Entity**

The National Aeronautics and Space Administration (NASA) is an independent Agency that was established by Congress on October 1, 1958 by the National Aeronautics and Space Act of 1958. NASA was incorporated from the Agency's predecessor organization, the National Advisory Committee for Aeronautics, which provided technical advice to the United States aviation industry and performed aeronautics research. Today, NASA serves as the fulcrum for initiatives by the U.S. in civil space and aviation.

As of August 2004, NASA is organized into four Business Lines which focus on the following objectives:

- **Exploration Systems:** creating new capabilities, supporting technologies and foundational research for affordable, sustainable human and robotic exploration;
- **Space Operations:** providing critical enabling technologies for much of the rest of NASA through the Space Shuttle, the International Space Station, and flight support;
- **Science:** exploring the Earth, moon, Mars, and beyond; charting the best route of discovery, and reaping the benefits of Earth and space exploration for society; and
- **Aeronautics Research:** conducting research that will enhance significantly aircraft performance, environmental compatibility, and safety, and that also will enhance the capacity, flexibility, and safety of the future air transportation system.

In addition, NASA has nine Business Line (Mission) Support Offices, including the Office of the Chief Financial Officer and Institutions & Management. The Agency's transformed structure includes a Strategic Management Council, an Operations Management Council and a Program Management Council to integrate NASA's strategic, tactical and operational decisions, and a number of new or reconstituted committees that support NASA's focus and direction. The transformed organizational structure is designed to streamline the Agency and position it to better implement the Vision for Space Exploration.

The nine NASA Centers, NASA Headquarters, and the Jet Propulsion Laboratory carry out the activities of the Mission Directorates. The Jet Propulsion Laboratory is a federally funded Research and Development Center owned by NASA but managed by an independent contractor.

The accompanying financial statements of NASA include the accounts of all funds which have been established and maintained to account for the resources under the control of NASA management.

**Basis of Accounting and Presentation**

These consolidated financial statements are prepared in accordance with generally accepted accounting principles (GAAP) in the United States of America as promulgated by the Federal Accounting Standards Advisory Board (FASAB) and the Office of Management and Budget (OMB) Circular A-136, Financial Reporting Requirements. FASAB is recognized by the American Institute of Certified Public Accountants (AICPA) as the official accounting standards-setting body of the United States government entities. The statements include the financial position, net cost of operations, changes in net position, budgetary resources, and financing of NASA, as required by the Chief Financial Officers Act of 1990 and the Government Management Reform Act of 1994.

The financial statements should be read with the realization they are a component of the U.S. government, a sovereign entity. One implication of this is that liabilities cannot be liquidated without legislation providing resources and legal authority to do so. The accounting structure of federal agencies is designed to reflect both accrual and budgetary accounting transactions. Under the accrual method of accounting, revenues are recognized when earned and expenses are recognized when a liability is incurred, without regard to receipt or payment of cash. Budgetary accounting facilitates compliance with legal constraints and controls over the use of federal funds.

**Budgets and Budgetary Accounting**

NASA follows standard Federal budgetary accounting policies and practices in accordance with OMB Circular A-11, Preparation, Submission and Execution of the Budget. Budgetary accounting facilitates compliance with legal constraints and controls over the use of Federal Funds. Congress funds NASA using three appropriations: Science, Aeronautics and Exploration; Exploration Capabilities; and Office of Inspector General.

**National Aeronautics and Space Administration**  
**Notes to Financial Statements**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**

**NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

The Science, Aeronautics and Exploration appropriation supports the following Business Lines: Science; Exploration Systems; and Aeronautics Research. The Exploration Capabilities appropriation supports the Space Operations Business Line which includes the Space Station, Space Shuttle, and Space and Flight Support. The Office of Inspector General appropriation funds the audit and investigation activities of the Agency.

Reimbursements to NASA appropriations are used to fund agreements between the Agency and other federal entities or the public. As part of its reimbursable program, NASA launches devices into space and provides tracking and data relay services for the U.S. Department of Defense, the National Oceanic and Atmosphere Administration, and the National Weather Service.

**Use of Estimates**

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

NASA requires major contractors to provide an estimate of their anticipated billing prior to their sending the actual invoice to the agency. In addition, NASA also requires the contractors to provide an estimate for the next month's anticipated work. When NASA receives these estimates they are compared to the contract under which the work is performed. If the estimate exceeds a specified funding line item the program manager and the procurement official, as necessary, review the estimate prior to posting in the general ledger as an estimated liability. If the review is not completed within the timeframe for quarterly or yearly reporting, the Agency uses the estimates of activity through the current period to establish an estimated liability, however, in this instance the agency fully recognizes that "no agency has the authority to pay liabilities not covered by budgetary resources." Liability to the contractor is not established by receipt of these estimates, but only when accepted by the Agency.

**Fund Balance with Treasury**

Treasury processes cash receipts and disbursements for NASA. Fund Balance with Treasury includes appropriated funds, trust funds, deposit funds, and budget clearing accounts.

**Investments in U.S. Government Securities**

Investments include the following Intragovernmental non-marketable securities:

- (1) National Aeronautics and Space Administration Endeavor Teacher Fellowship Trust Fund established from public donations in tribute to the crew of the Space Shuttle Challenger.
- (2) Science, Space and Technology Education Trust Fund established for programs to improve science and technology education.

**Accounts Receivable**

Most receivables are for reimbursement of research and development costs related to satellites and launch services. The allowance for uncollectible accounts is based upon evaluation of public accounts receivable, considering the probability of failure to collect based upon current status, financial and other relevant characteristics of debtors, and the relationship with the debtor. Under a cross-servicing agreement with the Department of Treasury, public accounts receivable over 180 days delinquent are turned over to Treasury for collection. The receivable remains on NASA's books until Treasury determines the receivable is uncollectible or the receivable is internally written off and closed out.

**Inventory and Related Property**

Inventory held by Centers and contractors that are repetitively procured, stored and issued on the basis of demand are considered Operating Materials and Supplies, a category of Inventory and Related Property. Certain NASA contractors' inventory management systems do not distinguish between items that should be classified as materials and those that should be classified as depreciable property. NASA reclassifies as property, all materials valued at \$100,000 or greater, in support of large-scale assets such as the Space Shuttle and the International Space Station.

**National Aeronautics and Space Administration**  
**Notes to Financial Statements**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**

**NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, CONTINUED**

**General Property, Plant and Equipment**

The Agency and its contractors and grantees hold NASA-owned property, plant, and equipment. Property with a unit cost of \$100,000 or more and a useful life of 2 years or more is capitalized; all other property is expensed when purchased. Capitalized costs include all costs incurred by NASA to bring the property to a form and location suitable for its intended use. Under provisions of the Federal Acquisition Regulation (FAR), contractors are responsible for control over accountability for Government-owned property in their possession. NASA's contractors and grantees report on NASA property in their custody annually and its top contractors report monthly.

Capitalized costs for internally developed software include the full costs (direct and indirect) incurred during the software development stage only. For purchased software, capitalized costs include amounts paid to vendors for the software and material internal costs incurred by the Agency to implement and make the software ready for use through acceptance testing. When NASA purchases software as part of a package of products and services (for example: training, maintenance, data conversion, reengineering, site licenses, and rights to future upgrades and enhancements), capitalized and non-capitalized costs of the package are allocated among individual elements on the basis of a reasonable estimate of their relative fair market values. Costs that are not susceptible to allocation between maintenance and relatively minor enhancements are expensed.

NASA capitalizes costs for internal use software when the total projected cost is \$1,000,000 or more and the expected useful life of the software is 2 years or more. These Financial Statements report depreciation expense using the straight-line method.

NASA began depreciating the International Space Station in FY 2001 when manned by the first permanent crew. Only the Station's major elements in space are depreciated; any on-ground elements are reported as Assets Under Construction (AUC) until launched and incorporated into the existing Station structure.

**Working Capital Fund**

Congress established the NASA Working Capital Fund (WCF) during fiscal year 2003 with the enactment of the FY 2003 Appropriations Act (P.L. 108-7). The Department of Treasury established a unique account for NASA that same fiscal year. During FY 2006 the NASA WCF consisted of two entities: 1) a Government-Wide Acquisition Contract (GWAC) that provides the latest in Information Technology (IT) products. This provided a simplified process for obtaining high-end commercial IT hardware and software at favorable prices through volume buying. 2) An agency-wide Service Center, NASA Shared Services Center (NSSC).

**NASA Shared Service Center**

NASA Shared Services Center opened March 1, 2006 on the grounds of Stennis Space Center. The NSSC is a public/private partnership between NASA and Computer Sciences Corporation Service Providers. The mixed staff of civil service and contractor personnel, performs a variety of consolidated transactional and administrative activities that were once carried out at each NASA center and Headquarters. These functions consisted of responsibilities in the following areas: Financial Management (FM), Human Resources (HR), Information Technology (IT) and Procurement.

**Liabilities Covered by Budgetary Resources**

Liabilities covered by budgetary resources are liabilities that are covered by realized budgetary resources as of the balance sheet date. Realized budgetary resources include new budget authority, unobligated balances of budgetary resources at the beginning of the year, and spending authority from offsetting collections. Examples include accounts payable and salaries. Accounts Payable includes amounts recorded for the receipt of goods or services furnished.

**Liabilities and Contingencies Not Covered by Budgetary Resources**

Generally liabilities not covered by budgetary resources are liabilities for which Congressional action is needed before budgetary resources can be provided. Examples include the Federal Employees' Compensation Act (FECA) actuarial liability and contingencies.

Liabilities not covered by budgetary resources include certain environmental matters, legal claims, pensions and other retirement benefits (ORB), workers' compensation, annual leave, and closed appropriations.



**National Aeronautics and Space Administration  
Notes to Financial Statements  
(Fiscal Years 2006 and 2005 Are Unaudited)**

**NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, CONTINUED**

**Reclassifications of 2005 Information**

Certain reclassifications have been made to Fiscal Year 2005 financial statements and footnotes to conform to OMB's changes to Circular A-136 effective in Fiscal Year 2006.

**Annual, Sick, and Other Leave**

Annual leave is accrued as it is earned; the accrual is reduced as leave is taken. Each year, the balance in the accrued annual leave account is adjusted to reflect current pay rates. To the extent current or prior year appropriations are not available to fund annual leave earned but not taken, funding will be obtained from future financing sources. Sick leave and other types of non-vested leave are expensed as taken.

**Federal Employee and Veterans' Benefits**

Agency employees participate in the Civil Service Retirement System (CSRS), a defined benefit plan, or the Federal Employees Retirement System (FERS), a defined benefit and contribution plan. For CSRS employees, NASA makes contributions of 8.51 percent of pay. For FERS employees, NASA makes contributions of 10.7 percent to the defined benefit plan, contributes 1 percent of pay to a retirement saving plan (contribution plan), and matches employee contributions up to an additional 4 percent of pay. For FERS employees, NASA also contributes to employer's matching share for Social Security.

Statement of Federal Financial Accounting Standards No. 5, "Accounting for Liabilities of the Federal Government," require Government agencies to report the full cost of employee health benefits (FEHB), and the Federal Employees Group Life Insurance (FEGLI) Programs. NASA used the applicable cost factors and imputed financing sources from the Office of Personnel and Management Letter For Chief Financial Officers, dated August 16, 2004, in these Financial Statements.

**Environmental and Disposal Liabilities**

The Agency records a liability for environmental and disposal clean-up costs from NASA operations that resulted in contamination from waste disposal methods, leaks, spills, and other past activity that created a public health or environmental risk. These liabilities are assessed by the engineers and finance staff to be probable, reasonably possible or remote. Mid-year determinations are made of the status of these unfunded liabilities and year end updates are made for any changes up or down that exceed \$200,000 and probable losses for which an estimate of remediation costs can be made are recorded. More details are also found in Note 10.

**National Aeronautics and Space Administration**  
**Notes to Financial Statements**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**

**NOTE 2. NON-ENTITY ASSETS**  
(In Millions of Dollars)

Non-Entity Assets are those assets that are held by NASA but are not available for use by NASA.

	2006	2005
Intragovernmental:		
Fund Balance with Treasury	\$ 1	\$ —
Accounts Receivable	2	5
<b>Total Intragovernmental</b>	<b>\$ 3</b>	<b>\$ 5</b>
Due from the Public:		
Accounts Receivable	—	11
<b>Total Non-Entity Assets</b>	<b>3</b>	<b>16</b>
Total Entity Assets	45,307	46,288
<b>Total Assets</b>	<b>\$ 45,310</b>	<b>\$ 46,304</b>

**National Aeronautics and Space Administration**  
**Notes to Financial Statements**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**

**NOTE 3. FUND BALANCE WITH TREASURY**  
(In Millions of Dollars)

Fund Balance with Treasury balance is the aggregate amount of all NASA agency location codes (ALC) accounts at Treasury, for which the agency is authorized to make expenditures and pay liabilities. The fund types are trust, appropriated and other funds.

Trust Funds include balances in Endeavor Teacher Fellowship Trust Fund, National Space Grant Program, Science, Space and Technology Education Trust Fund, and Gifts and Donations.

Appropriated Funds include balances in Space Flight Capabilities, Science, Aeronautics, and Exploration, Mission Support, Human Space Flight, Science, Aeronautics, and Technology, and Office of Inspector General.

Other Fund types include Fines, Penalties, and Forfeitures, General Fund Proprietary Interest, Working Capital Fund, Collections of Receivables from Canceled Appropriations, General Fund Proprietary Receipts, Budget Clearing and Suspense, Unavailable Check Cancellation, Undistributed Intergovernmental Payment, State and Local Taxes, Other Payroll, and US Employee Allotment Account, Savings Bonds.

**Fund Balances**

	2006	2005
Trust Funds	\$ 4	\$ 4
Appropriated Funds	9,542	8,169
Working Capital Fund	33	—
Other Fund Types	6	(27)
<b>Total</b>	<b>\$ 9,585</b>	<b>\$ 8,146</b>

The status of Fund Balance with Treasury represents the total fund balance as reflected in the general ledger for unobligated and obligated balances. Unobligated Balances—Available represent the amount remaining in appropriation accounts that are available for obligation in future fiscal years. Unobligated Balances—Unavailable represent the amount remaining in appropriation accounts that can only be used for adjustments to previously recorded obligations. Obligated Balances—Not Yet Disbursed represent the cumulative amount of obligations incurred, including accounts payable and advances from reimbursable customers, for which outlays have not been made.

**Status of Fund Balance with Treasury**

	2006	2005
Unobligated Balance		
Available	\$ 2,147	\$ 2,077
Unavailable	190	161
Obligated Balance Not Yet Disbursed	7,247	5,937
Clearing and Deposit Accounts	1	(29)
<b>Total</b>	<b>\$ 9,585</b>	<b>\$ 8,146</b>

**National Aeronautics and Space Administration**  
**Notes to Financial Statements**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**

**NOTE 4. INVESTMENTS**

(In Millions of Dollars)

Intragovernmental Securities are marketable federal securities bought and sold on the open market. The Bureau of the Public Debt issues non-marketable par value Treasury securities. The trust fund and cash balances are invested in Treasury securities, which are purchased and redeemed at par exclusively through Treasury's Federal Investment Branch. The effective-interest method was utilized to amortize discounts and premiums.

**As of September 30, 2006**

	<b>Cost</b>	<b>Amortization Method</b>	<b>Unamortized (Premium) Discount</b>	<b>Investments, Net</b>	<b>Market Value Disclosure</b>
<b>Intragovernmental Securities:</b>					
Non-Marketable:		Effective-interest			
Par Value	\$ 14	0.0431-8.875%	\$ 3	\$ 17	\$ 17
<b>Total</b>	<b>\$ 14</b>		<b>\$ 3</b>	<b>\$ 17</b>	<b>\$ 17</b>

**As of September 30, 2005**

	<b>Cost</b>	<b>Amortization Method</b>	<b>Unamortized (Premium) Discount</b>	<b>Investments, Net</b>	<b>Market Value Disclosure</b>
<b>Intragovernmental Securities:</b>					
Non-Marketable:		Effective-interest			
Par Value	\$ 14	0.0298-8.875%	\$ 3	\$ 17	\$ 17
<b>Total</b>	<b>\$ 14</b>		<b>\$ 3</b>	<b>\$ 17</b>	<b>\$ 17</b>

**National Aeronautics and Space Administration**  
**Notes to Financial Statements**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**

**NOTE 5. ACCOUNTS RECEIVABLE, NET**  
(In Millions of Dollars)

The Accounts Receivable balance includes receivables for reimbursement of research and development costs related to satellites and launch services. The allowance for uncollectible accounts is based upon evaluation of public accounts receivables, considering the probability of failure to collect based upon current status, financial and other relevant characteristics of debtors, and the relationship with the debtor.

The Accounts Receivable for September 30, 2006 and 2005, consist of the following:

**As of September 30, 2006**

	Accounts Receivable	Allowance for Uncollectible Accounts	Net Amount Due
Intragovernmental	\$ 180	\$ —	\$ 180
Public	6	(1)	5
<b>Total</b>	<b>\$ 186</b>	<b>\$ (1)</b>	<b>\$ 185</b>

**As of September 30, 2005**

	Accounts Receivable	Allowance for Uncollectible Accounts	Net Amount Due
Intragovernmental	\$ 136	\$ —	\$ 136
Public	61	(1)	60
<b>Total</b>	<b>\$ 197</b>	<b>\$ (1)</b>	<b>\$ 196</b>



**National Aeronautics and Space Administration**  
**Notes to Financial Statements**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**

**NOTE 6. INVENTORY AND RELATED PROPERTY, NET**  
(In Millions of Dollars)

Operating Materials and Supplies, Held for Use are tangible personal property held by NASA and its contractors to be used for fabricating and maintaining NASA assets and used in normal operations. Operating Materials and Supplies, Held in Reserve for Future Use are tangible personal property held by NASA for emergencies for which there is no normal recurring demand but that must be immediately available to preclude delay, which might result in loss, damage or destruction of Government property, danger to life or welfare of personnel, or substantial financial loss to the Government due to an interruption of operations.

All materials are valued using historical costs, or other valuation methods that approximate historical cost. Excess operating materials and supplies are materials that exceed the demand expected in the normal course of operations, and do not meet management's criteria to be held in reserve for future use. Obsolete operating material and supplies are materials no longer needed due to changes in technology, laws, customs, or operations. Unserviceable operating materials and supplies are materials damaged beyond economic repair.

	September 30, 2006	September 30, 2005
Inventory and Related Property, Net		
Operating Materials and Supplies		
Items Held for Use	\$ 2,687	\$ 3,401
Items Held in Reserve for Future Use	3	3
Excess, Obsolete, and Unserviceable	(360)	(385)
<b>Total</b>	<b>\$ 2,330</b>	<b>\$ 3,019</b>

**National Aeronautics and Space Administration**  
**Notes to Financial Statements**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**

**NOTE 7. GENERAL PROPERTY, PLANT, AND EQUIPMENT, NET**  
(In Millions of Dollars)

Theme Assets consist of assets specifically designed for use in a NASA program. Equipment includes special tooling, special test equipment, and Agency-peculiar property, such as the Space Shuttle and other configurations of spacecraft: engines, satellites, rockets, and other scientific components unique to NASA space programs. Structures, Facilities, and Leasehold Improvements include buildings with collateral equipment, and capital improvements, such as airfields, power distribution systems, flood control, utility systems, roads, and bridges. NASA also has use of certain properties at no cost. These properties include land at the Kennedy Space Center withdrawn from the public domain, land, and facilities at the Marshall Space Flight Center under a no cost 99-year lease with the U.S. Department of the Army. Work-in-Process (WIP) includes equipment and facilities that are being constructed. WIP includes the fabrication of assets that may or may not be capitalized once completed and operational. Projects that do not meet the capitalization criteria of two years of useful life and in excess of \$100,000 are expensed. All other project costs are capitalized in the year placed into operation.

NASA has International Space Station bartering agreements with international agencies including the European Space Agency and the National Space Agency of Japan. NASA barter with these space agencies to obtain International Space Station hardware elements in exchange for providing goods and services such as Space Shuttle transportation and a share of NASA's International Space Station utilization rights. The intergovernmental agreements state that the parties will seek to minimize the exchange of funds in the cooperative program, including the use of barter to provide goods and services. As of September 30, 2006, NASA has received some assets from these parties in exchange for future services. The fair value is indeterminable; therefore no value was ascribed to these transactions in accordance with APB No. 29, Accounting for Nonmonetary Transactions. Under all agreements to date, NASA's International Space Station Program's International Partners Office expects that NASA will eventually receive future NASA-required elements as well with no exchange of funds.

Prior to fiscal year 2006, President Bush announced a new vision for the Nation's space exploration program. Implementation of this initiative has required NASA to prioritize and restructure existing programs and missions, and to phase out or eliminate sooner than originally planned some programs and missions. These programs and missions include the Shuttle, which was originally planned to continue to the year 2020 but now will retire as soon as assembly of the International Space Station is completed (planned for the end of this decade). NASA will make an announcement in early FY 2007 regarding the future of planned servicing missions to the Hubble Space Telescope.

Management is exploring whether a significant portion of PP&E costs should be classified as research and development and therefore should be expensed. NASA is considering a change in its accounting policy for Theme Assets to reclassify some Theme Asset costs previously categorized as General Property, Plant, and Equipment (PP&E) as Research and Development (R&D) expenses. In the development of the revised policy, NASA followed standards established by the Financial Accounting Standards Board (FASB) in its Statement of Financial Accounting Standards No. 2, Accounting for Research and Development Costs. NASA believes that this change will result in financial reporting that is more relevant and timely to the readers of its financial statements. NASA requested that FASAB clarify the accounting standards the Agency used as the basis for its draft change in accounting policy. NASA anticipates a response from FASAB in FY 2007.

National Aeronautics and Space Administration  
Notes to Financial Statements  
(Fiscal Years 2006 and 2005 Are Unaudited)

**NOTE 7. GENERAL PROPERTY, PLANT, AND EQUIPMENT, NET (CONTINUED)**  
(In Millions of Dollars)

September 30, 2006

	Depreciation Method	Useful Life	Cost	Accumulated Depreciation	Book Value
<b>Government-owned/Government-held</b>					
Land			\$ 114	\$ —	\$ 114
Structures, Facilities and Leasehold Improvements	Straight-line	15–40 years	5,497	(4,082)	1,415
Theme Assets	Straight-line	2–20 years	43,593	(29,142)	14,451
Equipment	Straight-line	5–25 years	2,267	(1,644)	623
Internal Use Software and Development	Straight-line	5 years	139	(49)	90
Work-in-Process (WIP)					
Work-in-Process			204	—	204
Work-in-Process—Equipment			26	—	26
Assets Under Construction			8,198	—	8,198
<b>Total</b>			<b>\$ 60,038</b>	<b>\$ (34,917)</b>	<b>\$ 25,121</b>
<b>Government-owned/Contractor-held</b>					
Land			\$ 8	\$ —	\$ 8
Structures, Facilities and Leasehold Improvements	Straight-line	15–40 years	859	(704)	155
Equipment	Straight-line	5–25 years	12,264	(9,155)	3,109
Work-in-Process			4,800	—	4,800
<b>Total</b>			<b>\$ 17,931</b>	<b>\$ (9,859)</b>	<b>\$ 8,072</b>
<b>Total Property, Plant, and Equipment</b>			<b>\$ 77,969</b>	<b>\$ (44,776)</b>	<b>\$ 33,193</b>

National Aeronautics and Space Administration  
Notes to Financial Statements  
(Fiscal Years 2006 and 2005 Are Unaudited)

**NOTE 7. GENERAL PROPERTY, PLANT, AND EQUIPMENT, NET (CONTINUED)**  
(In Millions of Dollars)

September 30, 2005

	Depreciation Method	Useful Life	Cost	Accumulated Depreciation	Book Value
<b>Government-owned/Government-held</b>					
Land			\$ 114	\$ —	\$ 114
Structures, Facilities and Leasehold Improvements	Straight-line	15–40 years	5,567	(4,008)	1,559
Theme Assets	Straight-line	2–20 years	42,121	(25,699)	16,422
Equipment	Straight-line	5–25 years	2,109	(1,483)	626
Capitalized Leases	Straight-line	5–25 years	2	(1)	1
Internal Use Software and Development	Straight-line	5 years	89	(26)	63
Work-in-Process (WIP)					
Work-in-Process			199	—	199
Work-in-Process—Equipment			26	—	26
Assets Under Construction			6,953	—	6,953
<b>Total</b>			<b>\$ 57,180</b>	<b>\$ (31,217)</b>	<b>\$ 25,963</b>
<b>Government-owned/Contractor-held</b>					
Land			\$ 8	\$ —	\$ 8
Structures, Facilities and Leasehold Improvements	Straight-line	15–40 years	831	(628)	203
Equipment	Straight-line	5–25 years	10,921	(8,422)	2,499
Work-in-Process			6,253	—	6,253
<b>Total</b>			<b>\$ 18,013</b>	<b>\$ (9,050)</b>	<b>\$ 8,963</b>
<b>Total Property, Plant, and Equipment</b>			<b>\$ 75,193</b>	<b>\$ (40,267)</b>	<b>\$ 34,926</b>

**National Aeronautics and Space Administration**  
**Notes to Financial Statements**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**

**NOTE 8. LIABILITIES NOT COVERED BY BUDGETARY RESOURCES**  
(In Millions of Dollars)

Liabilities not covered by budgetary resources are liabilities for which Congressional action is needed before budgetary resources can be provided. They include certain environmental matters (Note 10), legal claims, pensions and other retirement benefits, workers' compensation, annual leave, and closed appropriations.

A liability was recorded for workers' compensation claims related to the Federal Employees' Compensation Act (FECA), administered by U.S. Department of Labor. The FECA provides income and medical cost protection to covered Federal civilian employees injured on the job, employees who have incurred a work-related occupational disease, and beneficiaries of employees whose death is attributable to a job-related injury or occupational disease. The FECA Program initially pays valid claims and subsequently seeks reimbursement from the Federal agencies employing the claimants.

The FECA liability includes the actuarial liability for estimated future costs of death benefits, workers' compensation, and medical and miscellaneous costs for approved compensation cases. The present value of these estimates at the end of fiscal year was calculated by the Department of Labor using a discount rate. This liability does not include the estimated future costs for claims incurred but not reported or approved as of the end of each year.

Fiscal Year	Discount Rate
2006	5.170%
2005	4.528%

NASA has recorded Accounts Payable related to closed appropriations for which there are contractual commitments to pay. These payables will be funded from appropriations available for obligation at the time a bill is processed, in accordance with Public Law 101-510.

	2006	2005
<b>Intragovernmental Liabilities:</b>		
Other Liabilities		
Workers' Compensation	\$ 15	\$ 15
Accounts Payable for Closed Appropriations	6	2
<b>Total Intragovernmental</b>	<b>\$ 21</b>	<b>\$ 17</b>
<b>Public Liabilities:</b>		
Accounts Payable		
Accounts Payable for Closed Appropriations	104	117
Federal Employee and Veterans Benefits		
Actuarial FECA Liability	60	62
Environmental and Disposal Liabilities	893	825
Other Liabilities		
Unfunded Annual Leave	179	171
Contingent Liabilities	4	5
<b>Total from the Public</b>	<b>\$ 1,240</b>	<b>\$ 1,180</b>
Total Liabilities Not Covered by Budgetary Resources	\$ 1,261	\$ 1,197
Total Liabilities Covered by Budgetary Resources	2,052	2,286
<b>Total Liabilities</b>	<b>\$ 3,313</b>	<b>\$ 3,483</b>



**National Aeronautics and Space Administration**  
**Notes to Financial Statements**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**

**NOTE 9. OTHER LIABILITIES**  
(In Millions of Dollars)

In FY 2006, NASA updated the format of this footnote to reflect changes made to the financial statement crosswalks issued by the Department of Treasury. In prior fiscal years, balances reported as Accounts Payable for Canceled Appropriations were reported on the Other Liabilities line of the Balance Sheet. This amount is currently reported on the Accounts Payable line of the Balance Sheet. Additionally, in previous fiscal years Actuarial FECA Liability was reported on the Balance Sheet line Other Liabilities. Currently, this amount is reported as separate line item on the Balance Sheet.

The format change from the September 30, 2005 published number was made to allow comparative data between 2005 and 2006.

**September 30, 2006**

	Current	Non-Current	Total
<b>Intragovernmental Liabilities</b>			
Advances from Others	\$ 114	\$ —	\$ 114
Workers' Compensation	15	—	15
Employer Contributions and Payroll Taxes	11	—	11
Liability for Deposit and Clearing Funds	14	—	14
Custodial Liability	8	—	8
Other Liabilities	(5)	—	(5)
<b>Total Intragovernmental</b>	<b>\$ 157</b>	<b>\$ —</b>	<b>\$ 157</b>
<b>Liabilities from the Public</b>			
Unfunded Annual Leave	\$ —	\$ 179	\$ 179
Employer Contributions and Payroll Taxes	17	—	17
Accrued Funded Payroll	70	—	70
Advances from Others	87	—	87
Contract Holdbacks	1	—	1
Custodial Liability	(17)	—	(17)
Other Accrued Liabilities	23	—	23
Contingent Liabilities	—	4	4
Liability for Deposit and Clearing Funds	(14)	—	(14)
Other Liabilities	5	—	5
<b>Total from the Public</b>	<b>\$ 172</b>	<b>\$ 183</b>	<b>\$ 355</b>
<b>Total Other Liabilities</b>	<b>\$ 329</b>	<b>\$ 183</b>	<b>\$ 512</b>

**National Aeronautics and Space Administration**  
**Notes to Financial Statements**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**

**NOTE 9. OTHER LIABILITIES (CONTINUED)**  
(In Millions of Dollars)

**September 30, 2005 (Restated)**

	Current	Non-Current	Total
<b>Intragovernmental Liabilities</b>			
Advances from Others	\$ 99	\$ —	\$ 99
Workers' Compensation	(1)	16	15
Employer Contributions and Payroll Taxes	10	—	10
Liability for Deposit and Clearing Funds	—	—	—
Custodial Liability	5	—	5
Other Liabilities	(5)	—	(5)
<b>Total Intragovernmental</b>	<b>\$ 108</b>	<b>\$ 16</b>	<b>\$ 124</b>
<b>Liabilities from the Public</b>			
Unfunded Annual Leave	\$ —	\$ 171	\$ 171
Employer Contributions and Payroll Taxes	6	—	6
Accrued Funded Payroll	71	—	71
Advances from Others	62	—	62
Contract Holdbacks	1	—	1
Custodial Liability	11	—	11
Other Accrued Liabilities	27	—	27
Contingent Liabilities	—	5	5
Liability for Deposit and Clearing Funds	(20)	—	(20)
Other Liabilities	6	—	6
<b>Total from the Public</b>	<b>\$ 164</b>	<b>\$ 176</b>	<b>\$ 340</b>
<b>Total Other Liabilities</b>	<b>\$ 272</b>	<b>\$ 192</b>	<b>\$ 464</b>

National Aeronautics and Space Administration  
Notes to Financial Statements  
(Fiscal Years 2006 and 2005 Are Unaudited)

**NOTE 10. ENVIRONMENT AND DISPOSAL LIABILITIES**  
(In Millions of Dollars)

Environmental and Disposal Liabilities represent cleanup costs from NASA operations that resulted in contamination from waste disposal methods, leaks, spills, and other past activity that created a public health or environmental risk. Federal, State, and local statutes and regulations require environmental cleanup costs. Some of these statutes are the Comprehensive Environmental Response, Compensation, and Liability Act; the Resource Conservation and Recovery Act; the Nuclear Waste Policy Act of 1982; and State and local laws.

Where up-to-date-site-specific engineering estimates for cleanup are not available, NASA employs commercially available parametric modeling software to estimate the total cost of cleaning up known contamination at these sites for current and future years. Several NASA centers have potential remediation issues that are not at this time measurable or estimable.

NASA recorded an unfunded liability in its financial statements to reflect the estimated total cost of environmental cleanup. This estimate could change in the future due to identification of additional contamination, inflation, deflation, and a change in technology or applicable laws and regulations as well as through ordinary liquidation of these liabilities as the cleanup program continues into the future. The estimate changed from FY 2005 to FY 2006 largely due to better information being available on the extent of contamination and remediation efforts that would be required. The estimate represents an amount that NASA expects to spend to remediate currently known contamination, subject to the availability of appropriated funds. Other responsible parties that may be required to contribute to the remediation funding could share this liability.

	FY 2006	FY 2005
Environmental Liabilities	\$ 893	\$ 825
<b>Total Environmental Cleanup</b>	<b>\$ 893</b>	<b>\$ 825</b>

In addition to the specific remediation efforts contemplated in the above estimates, NASA has a number of other potential remediation sites. For certain such sites, remediation costs ranging from \$7 million to \$65 million have been estimated as reasonably possible. Beyond acknowledging that such costs would be significant, for such other sites, management is not currently able to estimate the range of loss, or assess the likelihood that remediation efforts will be required.

**National Aeronautics and Space Administration**  
**Notes to Financial Statements**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**

**NOTE 11. CONTINGENT LIABILITIES**  
(In Millions of Dollars)

No balances have been recorded in the financial statements for contingencies related to proceedings, actions, and claims where management and legal counsel believe that it is possible but not probable that some costs will be incurred. There were certain cases that the lawyers reviewed and determined a loss was probable but could not estimate the amount of a future loss.

NASA is a party in various administrative proceedings, court actions (including tort suits), and claims brought by or against it. In the opinion of management and legal counsel, the ultimate resolution of these proceedings, actions, and claims will not materially affect the financial position, net cost, changes in net position, budgetary resources, or financing of NASA. Liabilities have been recorded for \$4 million and \$5 million for these matters as of September 30, 2006 and September 30, 2005, respectively.

**National Aeronautics and Space Administration**  
**Notes to Financial Statements**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**

**NOTE 12. INTRAGOVERNMENTAL COST AND EXCHANGE REVENUE**  
(In Millions of Dollars)

Intragovernmental costs and revenue are exchange transactions made between NASA and another Federal Government reporting entity. Costs and revenue with the Public result from transactions between NASA and a non-Federal entity. No comparison is available to the prior fiscal year due to a change in the data structure and a new method had not been established to format the information for disclosure for financial reporting. In August of 2004, NASA restructured from six strategic Enterprises to four Mission Directorates. The transformation did not provide sufficient lead time to develop the reporting structure in the financial management system for FY 2005.

	2006
<b>Science</b>	
Intragovernmental Costs	\$ 536
Public Cost	6,092
Total Science Costs	6,628
Intragovernmental Earned Revenue	350
Public Earned Revenue	(2)
Total Science Earned Revenue	348
<b>Total Science Net Cost</b>	<b>\$ 6,280</b>
<b>Exploration Systems</b>	
Intragovernmental Costs	\$ 214
Public Cost	2,490
Total Exploration Systems Costs	2,704
Intragovernmental Earned Revenue	89
Public Earned Revenue	(1)
Total Exploration Systems Earned Revenue	88
<b>Total Exploration Systems Net Cost</b>	<b>\$ 2,616</b>
<b>Aeronautics Research</b>	
Intragovernmental Costs	\$ 81
Public Cost	1,048
Total Aeronautics Research Costs	1,129
Intragovernmental Earned Revenue	63
Public Earned Revenue	16
Total Aeronautics Research Earned Revenue	79
<b>Total Aeronautics Research Net Cost</b>	<b>\$ 1,050</b>



**National Aeronautics and Space Administration**  
**Notes to Financial Statements**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**

**NOTE 12. INTRAGOVERNMENTAL COST AND EXCHANGE REVENUE (CONTINUED)**  
(In Millions of Dollars)

	2006
<b>Space Operations</b>	
Intragovernmental Costs	\$ 482
Public Cost	7,638
Total Space Operations Costs	<u>8,120</u>
Intragovernmental Earned Revenue	408
Public Earned Revenue	16
Total Space Operations Earned Revenue	<u>424</u>
<b>Total Space Operations Earned Net Cost</b>	<u>\$ 7,696</u>
<b>Net Cost of Operations</b>	<u>\$ 17,642</u>

**National Aeronautics and Space Administration**  
**Notes to Financial Statements**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**

**NOTE 13. UNDELIVERED ORDERS AT THE END OF THE PERIOD**  
(In Millions of Dollars)

Undelivered Orders at the end of the period total \$5,822 million and \$4,364 million as of September 30, 2006 and September 30, 2005, respectively. In previous fiscal years this amount was reported as a line item on the Statement of Budgetary Resources. Based on reporting changes as required by OMB A-136, undelivered orders is no longer reported on the statement. A footnote disclosure for total undelivered orders is required to comply with requirements of SFFAS 7.

Due to conversion differences in FY 2003, FACTS II unpaid obligations brought forward were adjusted by \$39 million in the current fiscal year. This adjustment is carried through the FY 2006 actual column of the Program and Financing Schedules reported in the FY 2008 Budget of the U.S. Government. Such information agrees with the related financial records and related data.

**NOTE 14. APPORTIONMENT CATEGORIES OF OBLIGATIONS INCURRED**  
(In Millions of Dollars)

Category A consists of amounts requested to be apportioned for each calendar quarter in the fiscal year. Category B consists of amounts requested to be apportioned on a basis other than calendar quarters, such as time periods other than quarters, activities, projects, objects, or a combination thereof.

	FY 2006	FY 2005
Direct Obligations:		
Category A	\$ 1	\$ 1
Category B	16,767	16,978
Reimbursable Obligations:		
Category B	1,005	1,019
<b>Total Obligations Incurred</b>	<b>\$ 17,773</b>	<b>\$ 17,998</b>

**NOTE 15. EXPLANATION OF DIFFERENCES BETWEEN THE SBR AND THE BUDGET OF THE U.S. GOVERNMENT**  
(In Millions of Dollars)

NASA compared the amounts reported on the Statement of Budgetary Resources and the actual amounts reported in the Budget of the United States Government as required by SFFAS No. 7 for FY 2005 and identified no material differences.

The Budget of the United States Government with actual amounts from FY 2006 was not published as of November 15, 2006. The comparison for FY 2006 will be performed when the Budget of the United States Government is published.

**NOTE 16. EXPLANATION OF DIFFERENCES BETWEEN LIABILITIES NOT COVERED BY BUDGETARY RESOURCES AND COMPONENTS REQUIRING OR GENERATING RESOURCES IN FUTURE PERIODS**  
(In Millions of Dollars)

Liabilities Not Covered by Budgetary Resources of \$1,261 and \$1,197 as of September 30, 2006 and September 30, 2005, respectively, represent NASA's environmental liability, FECA liability to Department of Labor and employees, contingent liabilities, accounts payable for closed appropriations and leave earned but not taken (See Note 8, Liabilities Not Covered by Budgetary Resources). Only a portion of these liabilities will require or generate resources in future periods.

**National Aeronautics and Space Administration**  
**Notes to Financial Statements**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**

**NOTE 17. STEWARDSHIP PP&E**  
(In Millions of Dollars)

Federal agencies are required to classify and report heritage assets, in accordance with the requirements of SFFAS No. 29, Heritage Assets and Stewardship Land.

Heritage Assets are property, plant, and equipment that possess one or more of the following characteristics: historical or natural significance; cultural, educational, or aesthetic value; or significant architectural characteristics.

Since the cost of heritage assets is usually not determinable, NASA does not value them or establish minimum value thresholds for designation of property, plant, or equipment as heritage assets. Additionally, the useful lives of heritage assets are not reasonably estimable for depreciation purposes. Since the most relevant information about heritage assets is their existence, they are qualified in terms of physical units, as follows:

	2005	Additions	Withdrawals	2006
Buildings and Structures	37	—	5	32
Air and Space Displays and Artifacts	492	4	—	496
Art and Miscellaneous Items	1,021	3	—	1,024
Total Heritage Assets	1,550	7	5	1,552

Heritage Assets were generally acquired through construction by NASA or its contractors, and are expected to remain in this category, except where there is legal authority for transfer or sale. Heritage assets are generally in fair condition, suitable only for display.

Many of the buildings and structures are designated as National Historic Landmarks. Numerous air and spacecraft and related components are on display at various locations to enhance public understanding of NASA programs. NASA eliminated their cost from its property records when they were designated as heritage assets. A portion of the amount reported for deferred maintenance is for heritage assets.

For more than 30 years, the NASA Art Program has documented America's major accomplishments in aeronautics and space. During that time, artists have generously contributed their time and talent to record their impressions of the U.S. Aerospace Program in paintings, drawings, and other media. Not only do these art works provide a historic record of NASA projects, they give the public a new and fuller understanding of advancements in aerospace. Artists give a special view of NASA through the back door. Some have witnessed astronauts in training or scientists at work. The art collection, as a whole, depicts a wide range of subjects, from Space Shuttle launches to aeronautics research, Hubble Space Telescope, and even virtual reality.

Artists commissioned by NASA receive a small honorarium in exchange for donating a minimum of one piece to the NASA archive. In addition, more works have been donated to the National Air and Space Museum.

In accordance with SFFAS No. 29 the cost of acquisition, improvement, reconstruction, or renovation of heritage assets is expensed in the period incurred.

In accordance with SFFAS No. 29, heritage assets that are used in day-to-day government operations are considered "multi-use" heritage assets that are not used for heritage purposes. Such assets are accounted for as general property, plant, and equipment and are capitalized and depreciated in the same manner as other general property, plant, and equipment. NASA has 45 buildings and structures that are considered to be multi-use heritage assets. The values of these assets are included in the property, plant, and equipment values shown in the Financial Statements.

**National Aeronautics and Space Administration**  
**Notes to Financial Statements**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**

**NOTE 18. GENERAL INFORMATION**  
(In Millions of Dollars)

During fiscal year 2003, NASA replaced ten disparate accounting systems and over 120 ancillary subsystems that had been in operation at our Centers for the past two decades, with a commercial off-the-shelf, Agency-wide, Integrated Financial Management system (SAP Core Financials application module).

Due to data anomalies in the FY 2003 conversion and known system limitations, NASA made a decision not to make prior period adjustments in fiscal years 2004 and 2005, and accordingly, processed all corrections in current year operations.

During fiscal year 2006, management recorded as current year expenses prior years property transactions for such items as equipment found during routine inventory processes, components of buildings removed and no longer in use, and the correction of manual processing errors.

In FY 2006, NASA continued to resolve a number of known reconciling items. Some resolutions required processing corrective transactions in the financial management system that impact line items on the financial statements.

**National Aeronautics and Space Administration**  
**Required Supplementary Stewardship Information**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**  
**Stewardship Investments: Research and Development**  
**For the Fiscal Year Ended September 30, 2006**  
(In Millions of Dollars)

**Research and Development Expenses by Business Lines**

In August 2004, NASA restructured from six strategic Enterprises to four Business Lines: Science, Exploration Systems, Aeronautics Research and Space Operations. Each Business Line is comprised of multiple themes and numerous programs comprise each theme. NASA's former enterprise structure has been mapped to the new Business Line structure and NASA will report Research and Development (R&D) expenses using the new structure. Therefore, R&D expenses will now be reported on a Program not Enterprise basis. This is NASA's first year reporting under this new structure. A description of NASA's R&D programs accompanies this reporting.

To provide the reader with a full picture of NASA expenses, both R&D and non-R&D, NASA has included expenses for non R&D costs associated with NASA activities such as Education and Outreach, Space Operations Programs. Descriptions for the work associated with these costs also accompany this reporting.



**National Aeronautics and Space Administration**  
**Required Supplementary Stewardship Information**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**  
**Stewardship Investments: Research and Development**  
**For the Fiscal Year Ended September 30, 2006**  
(In Millions of Dollars)

**Research and Development Expenses by Business Line by Theme by Program**

	2006
<b>Science</b>	
Solar System Exploration	
Discovery	\$ 127
New Frontiers	107
Technology	1,280
Deep Space Mission Systems (DSMS)	187
Solar System Research	321
Mars Exploration	599
<b>Solar System Exploration Total</b>	<b>\$ 2,621</b>
The Universe	
Navigator	\$ 87
James Webb Space Telescope	315
Hubble Space Telescope	452
Gamma-ray Large Space Telescope (GLAST)	87
Discovery	114
Explorer	58
Universe Research	225
International Space Science Collaboration	6
Beyond Einstein	8
<b>The Universe Total</b>	<b>\$ 1,352</b>
Earth-Sun System	
Earth Systematic Missions	\$ 293
Living with a Star	257
Solar Terrestrial Probes	95
Explorer Program	114
Earth System Science Pathfinder	104
Earth-Sun System Multi-Mission Operations	290
Earth-Sun Research	926
Applied Sciences	48
Earth-Sun Technology	82
<b>Earth-Sun System Total</b>	<b>\$ 2,209</b>
<b>Science Total</b>	<b>\$ 6,182</b>

**National Aeronautics and Space Administration**  
**Required Supplementary Stewardship Information**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**  
**Stewardship Investments: Research and Development (Continued)**  
**For the Fiscal Year Ended September 30, 2006**  
(In Millions of Dollars)

**Research and Development Expenses by Business Line by Theme by Program (Continued)**

	2006
<b>Exploration Systems</b>	
Constellation Systems	
Earth Orbit Capability	\$ 1,421
<b>Constellations Systems Total</b>	<b>\$ 1,421</b>
Exploration Systems Research & Technology	
Advanced Space Technology	3
Technology Maturation	111
Robotic Lunar Exploration	95
<b>Exploration Systems Research &amp; Technology Total</b>	<b>\$ 209</b>
Prometheus Nuclear Systems & Technology	
Advanced Systems and Technology	291
Nuclear Flight Systems	24
<b>Prometheus Systems Research &amp; Technology Total</b>	<b>\$ 315</b>
Human Systems Research & Technology	
Life Support & Habitation	361
Human Health & Performance	136
Human Systems Integration	174
<b>Human Systems Research &amp; Technology Total</b>	<b>\$ 671</b>
<b>Exploration Systems Total</b>	<b>\$ 2,616</b>
<b>Aeronautics</b>	
Aeronautics Technology	
Aviation Safety Program	152
Airspace Systems	144
Fundamental Aeronautics	754
<b>Aeronautics Technology Total</b>	<b>\$ 1,050</b>
<b>Aeronautics Total</b>	<b>\$ 1,050</b>
<b>Total Research &amp; Development Expenses</b>	<b>\$ 9,848</b>

National Aeronautics and Space Administration  
Required Supplementary Stewardship Information  
(Fiscal Years 2006 and 2005 Are Unaudited)  
Stewardship Investments: Research and Development (Continued)  
For the Fiscal Year Ended September 30, 2006  
(In Millions of Dollars)

Non-Research and Development Expenses by Business Line by Theme by Program

	2006
<b>Science</b>	
Earth-Sun System	
Education and Outreach	\$ 40
SOFIA	58
<b>Science Total</b>	<u>\$ 98</u>
<b>Space Operations</b>	
Space Shuttle	4,245
International Space Station	1,708
Space and Flight Support (SFS)	1,743
<b>Space Operations Total</b>	<u>\$ 7,696</u>
<b>Total Non-Research &amp; Development Expenses</b>	<u>\$ 7,794</u>
<b>Total Expenses</b>	<u><u>\$ 17,642</u></u>

**National Aeronautics and Space Administration**  
**Required Supplementary Stewardship Information**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**  
**Stewardship Investments: Research and Development (Continued)**  
**For the Fiscal Year Ended September 30, 2006**  
(In Millions of Dollars)

NASA makes substantial research and development investments for the benefit of the United States. These amounts are expensed as incurred in determining the net cost of operations.

NASA's research and development programs include activities to extend our knowledge of Earth, its space environment, and the universe, and to invest in new aeronautics and advanced space transportation technologies that support the development and application of technologies critical to the economic, scientific, and technical competitiveness of the United States.

Investment in research and development refers to those expenses incurred to support the search for new or refined knowledge and ideas and for the application or use of such knowledge and ideas for the development of new or improved products and processes with the expectation of maintaining or increasing national economic productive capacity or yielding other future benefits. Research and development is composed of the following:

Basic Research: Systematic study to gain knowledge or understanding of the fundamental aspects of phenomena and of observable facts without specific applications toward processes or products in mind;

Applied Research: Systematic study to gain knowledge or understanding necessary for determining the means by which a recognized and specific need may be met; and

Development: Systematic use of the knowledge and understanding gained from research for the production of useful materials, devices, systems or methods, including the design and development of prototypes and processes.

## **Business Line Theme and Program Descriptions**

### **BUSINESS LINE: SCIENCE**

#### **Theme: Solar System Exploration**

The Solar System Exploration (SSE) Theme seeks to understand how the solar system formed and evolved, and whether there might be life in the solar system beyond Earth.

##### **Program: Discovery**

NASA's Discovery program represents a breakthrough in the way NASA explores space, with lower-cost, highly focused planetary science investigations designed to enhance our understanding of the solar system.

##### **Program: New Frontiers**

The New Frontiers program, a class of competed medium-sized missions, represents a critical step in the advancement of the solar system exploration. Proposed science targets for the New Frontiers program include Pluto and the Kuiper Belt, Jupiter, Venus, and sample returns from Earth's Moon and a comet nucleus.

##### **Program: Technology**

Robotic spacecraft use electrical power for propulsion, data acquisition, and communication to accurately place themselves in orbit around and onto the surfaces of bodies about which we may know relatively little. These systems ensure that they survive and function in hostile and unknown environments, acquire and transmit data throughout their lifetimes, and sometimes transport samples back to Earth. Since successful completion of these missions is so dependent on power, the future SSE portfolio of missions will demand advances in power and propulsion systems.

##### **Program: Deep Space Mission System (DSMS)**

This program seeks to enable NASA exploration, both human and robotic, of the solar system and beyond by providing reliable, high performance, and cost effective telecommunications and navigation services to its lunar and deep space missions.

##### **Program: Solar Systems Research**

The Solar System Exploration (SSE) Research Program develops the theoretical tools and laboratory data needed to analyze flight data, makes possible new and better instruments to fly on future missions, and analyzes the data returned so that SSE can answer specific questions posed and fit this new knowledge into the overall picture of the solar system.

**National Aeronautics and Space Administration**  
**Required Supplementary Stewardship Information**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**  
**Stewardship Investments: Research and Development (Continued)**  
**For the Fiscal Year Ended September 30, 2006**  
(In Millions of Dollars)

**Program: Mars Exploration**

The Mars Exploration Program has been developed to conduct a rigorous, incremental, discovery-driven exploration of Mars to determine the planet's physical, dynamic, and geological characteristics, investigate the Martian climate in the context of understanding habitability, and investigate whether Mars ever had the potential to develop and harbor any kind of life.

**Theme: The Universe**

The Universe Theme supports NASA's mission to "explore the universe and search for life" by attempting to understand the origin and evolution of life, searching for evidence of life elsewhere and exploring the universe beyond.

**Program: Navigator**

The Navigator program consists of a coherent series of increasingly challenging projects, each complementary to the others and each mission building on the results and capabilities of those that preceded it as NASA searches for habitable planets outside of the solar system.

**Program: The James Webb Space Telescope (JWST)**

The program identified by the National Research Council as the top priority for astronomy and physics for the current decade—is a large, deployable infrared astronomical space-based observatory. The mission is a logical successor to the HST, extending beyond Hubble's discoveries into the infrared, where the highly redshifted early universe must be observed, where cool objects like protostars and protoplanetary disks emit strongly, and where dust obscures shorter wavelengths.

**Program: Hubble Space Telescope**

Since 1990, the HST has used its pointing precision, powerful optics, and state-of-the-art instruments to explore the visible, ultraviolet and near-infrared regions of the electromagnetic spectrum. Until such time that Hubble is no longer able to carry out its scientific mission, the observatory will continue to investigate the formation, structure, and evolution of stars and galaxies, studying the history of the universe, and providing a space-based research facility for optical astronomy.

Hubble development funding supports a suite of life extension activities, which will maximize science return as the telescope's capabilities degrade over time. In addition, a robotic spacecraft is under development to be launched on an expendable launch vehicle, rendezvous with HST, and safely deorbit the observatory at the end of its useful science life. While this development activity is underway, modification and upkeep of ground operations systems will continue.

**Program: Gamma-ray Large Area Space Telescope (GLAST)**

A collaboration with the Department of Energy, France, Italy, Sweden, Japan, and Germany, the Gamma-ray Large Area Space Telescope (GLAST) will improve researchers' understanding of the structure of the universe, from its earliest beginnings to its ultimate fate. By measuring the direction, energy, and arrival time of celestial high-energy gamma rays, GLAST will map the sky with 50 times the sensitivity of previous missions, with corresponding improvements in resolution and coverage. Yielding new insights into the sources of high-energy cosmic gamma rays, GLAST will reveal the nature of astrophysical jets and relativistic flows and study the sources of gamma-ray bursts.

**Program: Discovery**

The Discovery program gives scientists the opportunity to dig deep into their imaginations and find innovative ways to unlock the mysteries of the solar system. Discovery is an ongoing program that offers the scientific community the opportunity to assemble a team and design exciting, focused science investigations that complement NASA's larger planetary science explorations.

**Program: Explorer**

The Explorer program provides frequent flight opportunities for world-class astrophysics and space physics investigations, utilizing innovative, streamlined and efficient management approaches to spacecraft development and operations. The program (including Future Explorers) is managed within the Earth-Sun Theme, but selected projects are managed under the Universe Theme.

**National Aeronautics and Space Administration**  
**Required Supplementary Stewardship Information**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**  
**Stewardship Investments: Research and Development (Continued)**  
**For the Fiscal Year Ended September 30, 2006**  
(In Millions of Dollars)

**Program: Universe Research**

The Universe Theme's Research program strives to answer critical questions about the nature of the universe with a host of operating missions led by investigators from academia and industry, as well as funding grants for basic research, technology development, and data analysis from past and current missions. All data collected by missions are archived in data centers located at universities and NASA centers throughout the country.

**Program: International Space Science Collaboration (SSC)**

Herschel and Planck, two projects in the International Space Science Collaboration (SSC) Program, are European Space Agency (ESA)-led missions. Herschel has been designed to unveil a face of the early universe that has remained hidden until now. Planck will help provide answers to one of the most important sets of questions asked in modern science: how did the universe begin, how did it evolve to the state we observe today, and how will it continue to evolve in the future?

**Program: Beyond Einstein**

Beyond Einstein (BE) flagship missions are the Laser Interferometer Space Antenna (LISA) & Constellation-X (Con-X). LISA, a joint effort NASA/ESA effort, will be the first space-based gravitational wave observatory. LISA will study the death spirals of stars, colliding black holes, and echoes from the universe all the way back to the Big Bang. Con-X will be a combination of several separate spacecraft working in unison as 1 giant X-ray telescope far more powerful than any previous. Con-X will investigate black holes, galaxy formation, the evolution of the universe on the largest scales, the recycling of matter and energy, and the nature of "dark matter."

**Theme: Earth–Sun System**

NASA uses the unique vantage point of space to understand and explore Earth and the Sun. The relationship between the Sun and the Earth is at the heart of a complex, dynamic system that researchers do not yet fully understand. The Earth–Sun system, like the human body, is comprised of diverse components that interact in complex ways, requiring unique capabilities for characterizing, understanding, and predicting change. Therefore, researchers need to understand the Sun, the heliosphere, and Earth's atmosphere, lithosphere, hydrosphere, cryosphere, and biosphere as a single connected system.

**Program: Earth Systematic Missions**

Earth Systematic Missions provide Earth observing satellites that contribute to the provision of long-term environmental data sets that can be used to study the evolution of the Earth system on a range of temporal scales. This information is used to analyze, model, and improve understanding of the Earth system.

**Program: Living with a Star**

The Living With a Star (LWS) program seeks to understand how and why the Sun varies, how Earth and other planets respond, and how the variability and response affect humanity. Achieving these goals will enable a reliable space weather prediction so undesirable space weather effects can be accommodated or mitigated before they occur.

**Program: Solar Terrestrial Probes (STP)**

The primary goal of the Solar Terrestrial Probes (STP) Program is to understand how the Sun, heliosphere, and planetary environments are connected in a single system.

**Program: Explorer**

The mission of the Explorer program is to provide frequent flight opportunities for world-class astrophysics and space physics investigations, utilizing innovative, streamlined and efficient management approaches to spacecraft development and operations.

**Program: Earth System Science Pathfinder (ESSP)**

This program addresses unique, specific, highly-focused mission requirements in Earth science research. ESSP includes a series of relatively low to moderate cost, small to medium sized, competitively selected, principal investigator led missions that are built, tested, and launched in a short time interval. These missions are capable of supporting a variety of scientific objectives related to Earth science, involving the atmosphere, oceans, land surface, polar ice regions and solid earth.

**National Aeronautics and Space Administration**  
**Required Supplementary Stewardship Information**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**  
**Stewardship Investments: Research and Development (Continued)**  
**For the Fiscal Year Ended September 30, 2006**  
(In Millions of Dollars)

**Program: Earth–Sun System Multi-Mission Operations**

This program acquires, preserves, and delivers the observation data for the Science Mission Directorate/Earth–Sun System scientific focus areas in conformance with national science objectives.

**Program: Earth–Sun System Division (ESSD)**

The program observations and research aim to improve our capability for predicting weather, climate and natural hazards, including space weather. The focus of NASA's efforts in ESSD is the development and demonstration of space-based measurements, providing information about the Earth–Sun system not available by other means.

**Program: Applied Sciences**

The Applied Sciences program bridges the gap between scientific discoveries and practical applications that benefit society through partnerships that integrate the observations and predictions resulting from NASA Earth–Sun system science into solutions.

**Program: Earth–Sun System Education and Outreach**

The program uses NASA's results from studying the Earth system and the Sun to enhance the teaching and learning of Earth, space, and environmental sciences through partnerships with educational institutions and organizations.

**Program: Earth–Sun Technology**

NASA's ESSD is dedicated to understanding the total Earth–Sun system and the effects of natural and human-induced changes on the global environment.

**BUSINESS LINE: EXPLORATION SYSTEMS**

**Theme: Constellation Systems**

Through the Constellation Systems Theme NASA will develop, demonstrate, and deploy the collection of systems that will enable sustained human and robotic exploration of the Moon, Mars, and beyond.

**Program: Earth Orbit Capability**

The Earth Orbit Capability program is responsible for developing, demonstrating, and deploying the capability for crew transportation to Earth orbit.

**Theme: Exploration Systems Research and Technology**

The Exploration Systems Research and Technology (ESR&T) Theme represents NASA's commitment to investing in the technologies and capabilities that will make the national vision for space exploration possible.

**Program: Advanced Space Technology**

The Advanced Space Technology program develops new technologies that will enable NASA to conduct new human and robotic exploration missions, gather new types of scientific data, and reduce mission risk and cost.

**Program: Technology Maturation**

The Technology Maturation program develops and validates the most promising advanced space technology concepts and matures them to the level of demonstration and space flight validation, to enable safe, affordable, effective and sustainable human-robotic exploration.

**Program: Robotic Lunar Exploration (RLE)**

This program will undertake lunar exploration activities that enable sustained human and robotic exploration of the Moon. These activities will further science, and develop and test new approaches, technologies, and systems, including use of lunar and other space resources, to support sustained human space exploration.

**Theme: Prometheus Nuclear Systems and Technology**

Prometheus Nuclear Systems and Technology represents NASA's effort to develop an advanced technology capability for more complex operations and exploration of the solar system.



**National Aeronautics and Space Administration**  
**Required Supplementary Stewardship Information**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**  
**Stewardship Investments: Research and Development (Continued)**  
**For the Fiscal Year Ended September 30, 2006**  
(In Millions of Dollars)

**Program: Advanced Systems and Technology**

The Advanced Systems and Technology program develops and demonstrates advanced nuclear technologies and engineered systems. This technology development will be necessary to support NASA's goal of more distant, more ambitious, and longer duration human and robotic exploration of Mars and other destinations.

**Program: Nuclear Flight Systems**

The Nuclear Flight Systems program continues NASA's development of nuclear reactor power and associated spacecraft systems to enhance NASA's abilities to conduct robotic exploration and science operations.

**Theme: Human Systems Research and Technology**

This Theme focuses on ensuring the health, safety, and security of humans through the course of solar system exploration.

**Program: Life Support and Habitation**

The Life Support and Habitation program focuses on enabling human exploration beyond low Earth orbit by developing technologies to support human activity in and beyond low Earth orbit.

**Program: Human Health and Performance**

The Human Health and Performance program delivers research, technology, knowledge, and tools that will enable human space exploration. Specifically, the Human Health and Performance program will guide the development of various countermeasures to aid astronauts counteract any deleterious effects of long-duration missions in the space environment; develop tools and techniques to improve medical care delivery to space exploration crews; increase our biomedical knowledge and improve understanding of radiation effects to reduce the uncertainty in estimating space radiation health risks to human crews; and, acquire new information in exploration biology, which will identify and define the scope of problems that will face future human space explorers during long periods of exposure to space.

**Program: Human Systems Integration**

The Human-Systems Integration program conducts research and technology development driven by Agency needs for crew health; design of human spacecraft, space suits, and habitats; efficient crew operations; medical operations; and technology development to enable safe and productive human space exploration.

**BUSINESS LINE: AERONAUTICS RESEARCH**

**Theme: Aeronautics Technology (AT)**

Aeronautics Technology conducts high-quality, innovative research that will lead to revolutionary concepts, technologies, and capabilities that enable radical change to both the airspace system and the aircraft that fly within it.

**Program: Aviation Safety**

The Aviation Safety program builds upon the unique safety-related research capabilities of NASA to develop tools, methods, and technologies that will improve the intrinsic safety attributes of current and future aircraft, and to overcome aircraft safety technological barriers that would otherwise constrain the full realization of Next Generation Air Transportation System (NGATS).

**Program: Airspace Systems**

The Airspace Systems Program conducts cutting-edge air traffic management research that will enable the NGATS. In partnership with the Joint Planning and Development Office (JPDO), the ASP will help develop the concepts, capabilities and technologies that will lead to the significant enhancements in capacity, efficiency and flexibility needed to meet the Nation's airspace and airport requirements for decades to come.

**National Aeronautics and Space Administration**  
**Required Supplementary Stewardship Information**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**  
**Stewardship Investments: Research and Development (Continued)**  
**For the Fiscal Year Ended September 30, 2006**  
(In Millions of Dollars)

**Program: Fundamental Aeronautics**

The Fundamental Aeronautics program will conduct cutting-edge research that will enable the design of vehicles that fly through any atmosphere at any speed. Because aircraft of the future will need to address multiple and often conflicting design challenges such as noise, emissions, and performance, a key focus will be the development of physics-based, multidisciplinary design, analysis, and optimization (MDAO) tools. Such tools will make it possible to evaluate radically new vehicle designs and to assess, with known uncertainties, the potential impact of innovative concepts and technologies on a vehicle's overall performance.

**NON-R&D Programs**

**BUSINESS LINE: SCIENCE**

**Theme: Earth–Sun System**

**Program: Education and Outreach**

The program uses NASA's results from studying the Earth system and the Sun to enhance the teaching and learning of Earth, space, and environmental sciences through partnerships with educational institutions and organizations.

**Program: SOFIA**

Stratospheric Observatory for Infrared Astronomy (SOFIA) is a telescope mounted onto a specially designed Boeing 747. The project has considered the use of SOFIA as a platform for pursuits other than its primary mission of astronomy/astro-physics. According to SOFIA's Project Manager, a concept has been developed for SOFIA to be used for Earth Science investigations, simultaneously with SOFIA's prime mission. Also, additional in depth studies include using SOFIA as an experimental platform to test high bandwidth communications with Mars spacecraft or as a testbed for high-bandwidth earth communications.

**BUSINESS LINE: SPACE OPERATIONS**

**Theme: Space Shuttle**

The Space Shuttle is currently the only launch capability owned by the United States that enables human access to space, and the only vehicle that can support the assembly of the International Space Station (ISS). NASA will phase-out the Space Shuttle in 2010 when its role in ISS assembly is complete.

**Theme: International Space Station**

This Theme supports the construction and operations of a research facility in low Earth orbit as NASA's first step in achieving the Vision for Space Exploration. The ISS provides a unique, continuously operating capability to develop medical countermeasures for long-term human space travel; develop and test technologies and engineering solutions in support of exploration; and provide ongoing practical experience in living and working in space. It also supports a variety of pure and applied research for the U.S. and its International Partners. ISS assembly will be completed by the end of the decade. NASA is examining configurations for the Space Station that meet the needs of both the new space exploration vision and our international partners using as few Shuttle flights as possible. A key element of the ISS program is the crew and cargo services project, which will purchase services for cargo and crew transport using existing and emerging capabilities.

**Theme: Space and Flight Support**

This theme encompasses Space Communications, Launch Services, Rocket Propulsion Testing, and Crew Health and Safety. Space Communications consists of (1) the Tracking and Data Relay Satellite System (TDRSS), which supports activities such as the Space Shuttle, ISS, Expendable Launch Vehicles, and research aircraft, and (2) the NASA Integrated Services Network, which provides telecommunications services at facilities, such as flight support networks, mission control centers and science facilities, and administrative communications networks for NASA Centers. The Launch Services program focuses on meeting the Agency's launch and payload processing requirements by assuring safe and cost-effective access to space via the Space Shuttle and expendable launch vehicles.

**National Aeronautics and Space Administration**  
**Required Supplementary Information**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**  
**Combined Schedule of Budgetary Resources**  
**For the Fiscal Year Ended September 30, 2006**  
(In Millions of Dollars)

	Exploration, Science, and Aeronautics	Exploration Capabilities	Office of Inspector General	Other	Total
<b>Budgetary Resources</b>					
Unobligated Balance, Brought Forward, October 1	1,245	840	4	152	2,241
Recoveries of Prior Year Obligations	183	105	—	80	368
Budget Authority:					
Appropriation	9,761	7,048	32	2	16,843
Spending Authority from Offsetting Collections					
Earned					
Collected	598	360	—	31	989
Change in Receivable from Federal Sources	11	35	—	(5)	41
Change in Unfilled Orders					
Advance Received	36	8	—	13	57
Without Advance from Federal Sources	(129)	(81)	—	2	(208)
Subtotal	10,277	7,370	32	43	17,722
Nonexpenditure Transfers, Net:					
Actual Transfers, Budget Authority	85	(59)	—	—	26
Permanently Not Available					
Cancellations of Expired and No-year Accounts	—	—	—	(37)	(37)
Enacted Reductions	(125)	(85)	—	—	(210)
<b>Total Budgetary Resources</b>	<b>\$ 11,665</b>	<b>\$ 8,171</b>	<b>\$ 36</b>	<b>\$ 238</b>	<b>\$ 20,110</b>
<b>Status of Budgetary Resources</b>					
Obligations Incurred:					
Direct:	9,630	7,047	32	59	16,768
Reimbursable:	578	384	—	43	1,005
Total Obligations Incurred	10,208	7,431	32	102	17,773
Unobligated Balance:					
Apportioned	1,403	707	—	33	2,143
Exempt from Apportionment	—	—	—	4	4
Total Unobligated Balances	1,403	707	—	37	2,147
Unobligated Balance Not Available	54	33	4	99	190
<b>Total Status of Budgetary Resources</b>	<b>\$ 11,665</b>	<b>\$ 8,171</b>	<b>\$ 36</b>	<b>\$ 238</b>	<b>\$ 20,110</b>

**National Aeronautics and Space Administration**  
**Required Supplementary Information**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**  
**Combined Schedule of Budgetary Resources**  
**For the Fiscal Year Ended September 30, 2006 (Continued)**  
(In Millions of Dollars)

	Exploration, Science, and Aeronautics	Exploration Capabilities	Office of Inspector General	Other	Total
<b>Change in Obligated Balance</b>					
Obligated Balances, Net, October 1	3,454	1,950	6	563	5,973
Obligations Incurred, Net	10,209	7,431	32	101	17,773
Less: Gross Outlays	8,486	7,484	33	256	16,259
Less: Recoveries of Prior Year Unpaid Obligations	183	105	—	80	368
Change in Uncollected Customer Payments from Federal Sources	118	46	—	3	167
Obligated Balance, Net, End of Period					
Unpaid Obligations	5,343	1,984	5	339	7,671
Less: Uncollected Customer Payments from Federal Sources	231	146	—	8	385
<b>Total, Unpaid Obligated Balance, Net, End of Period</b>	<b>\$ 5,112</b>	<b>\$ 1,838</b>	<b>\$ 5</b>	<b>\$ 331</b>	<b>\$ 7,286</b>
<b>Outlays</b>					
Net Outlays					
Gross Outlays	8,486	7,484	33	256	16,259
Less: Offsetting Collections	633	367	—	45	1,045
Subtotal	7,853	7,117	33	211	15,214
Less: Distributed Offsetting Receipts	—	—	—	8	8
<b>Net Outlays</b>	<b>\$ 7,853</b>	<b>\$ 7,117</b>	<b>\$ 33</b>	<b>\$ 203</b>	<b>\$ 15,206</b>

**National Aeronautics and Space Administration**  
**Required Supplementary Information**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**  
**Combined Schedule of Budgetary Resources**  
**For the Fiscal Year Ended September 30, 2005**  
(In Millions of Dollars)

	Exploration, Science, and Aeronautics	Exploration Capabilities	Office of Inspector General	Other	Total
<b>Budgetary Resources</b>					
Unobligated Balance, Brought Forward, October 1	1,203	560	—	1,338	3,101
Recoveries of Prior Year Obligations	—	—	—	10	10
Budget Authority:					
Appropriation	7,743	8,552	32	(12)	16,315
Spending Authority from Offsetting Collections					
Earned					
Collected	476	338	—	37	851
Change in Receivable from Federal Sources	25	8	—	(12)	21
Change in Unfilled Orders					
Advance Received	—	15	—	(5)	10
Without Advance from Federal Sources	26	107	—	(16)	117
Subtotal	8,270	9,020	32	(8)	17,314
Nonexpenditure Transfers, Net:					
Actual Transfers, Budget Authority	197	(197)	—	—	—
Permanently Not Available					
Cancellations of Expired and No-year Accounts	—	—	—	(60)	(60)
Enacted Reductions	(62)	(67)	—	—	(129)
<b>Total Budgetary Resources</b>	<b>\$ 9,608</b>	<b>\$ 9,316</b>	<b>\$ 32</b>	<b>\$ 1,280</b>	<b>\$ 20,236</b>
<b>Status of Budgetary Resources</b>					
Obligations Incurred:					
Direct:	7,817	8,088	29	1,045	16,979
Reimbursable:	546	388	—	85	1,019
Total Obligations Incurred	8,363	8,476	29	1,130	17,998
Unobligated Balance:					
Apportioned	1,270	771	2	30	2,073
Exempt from Apportionment	—	—	—	4	4
Total Unobligated Balances	1,270	771	2	34	2,077
Unobligated Balance Not Available	(25)	69	1	116	161
<b>Total Status of Budgetary Resources</b>	<b>\$ 9,608</b>	<b>\$ 9,316</b>	<b>\$ 32</b>	<b>\$ 1,280</b>	<b>\$ 20,236</b>

**National Aeronautics and Space Administration**  
**Required Supplementary Information**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**  
**Combined Schedule of Budgetary Resources**  
**For the Fiscal Year Ended September 30, 2005, Continued**  
(In Millions of Dollars)

	Exploration, Science, and Aeronautics	Exploration Capabilities	Office of Inspector General	Other	Total
<b><u>Change in Obligated Balance</u></b>					
Obligated Balances, Net, October 1	2,567	1,687	4	301	4,559
Obligations Incurred, Net	8,363	8,476	29	1,130	17,998
Less: Gross Outlays	7,433	8,095	28	916	16,472
Less: Recoveries of Prior Year Unpaid Obligations	—	—	—	10	10
Change in Uncollected Customer Payments from Federal Sources	(51)	(115)	—	28	(138)
Obligated Balance, Net, End of Period					
Unpaid Obligations	3,795	2,145	5	543	6,488
Less: Uncollected Customer Payments from Federal Sources	349	192	—	10	551
<b>Total, Unpaid Obligated Balance, Net, End of Period</b>	<b>\$ 3,446</b>	<b>\$ 1,953</b>	<b>\$ 5</b>	<b>\$ 533</b>	<b>\$ 5,937</b>
<b><u>Outlays</u></b>					
Net Outlays:					
Gross Outlays	7,433	8,095	28	916	16,472
Less: Offsetting Collections	476	352	—	33	861
Subtotal	6,957	7,743	28	883	15,611
Less: Distributed Offsetting Receipts	—	—	—	—	—
<b>Net Outlays</b>	<b>\$ 6,957</b>	<b>\$ 7,743</b>	<b>\$ 28</b>	<b>\$ 883</b>	<b>\$ 15,611</b>

**National Aeronautics and Space Administration**  
**Required Supplementary Information**  
**(Fiscal Years 2006 and 2005 Are Unaudited)**  
**Deferred Maintenance**  
**For the Fiscal Year Ended September 30, 2006**

NASA has deferred maintenance only on its facilities, including structures. There is no significant deferred maintenance on other physical property, such as land, equipment, theme assets, leasehold improvements, or assets under capital lease. Contractor-held property is subject to the same considerations.

NASA developed a Deferred Maintenance parametric estimating method (DM method) in order to conduct a consistent condition assessment of its facilities. This method was developed to measure NASA's current real property asset condition and to document real property deterioration. The DM method produces both a parametric cost estimate of deferred maintenance, and a Facility Condition Index. Both measures are indicators of the overall condition of NASA's facility assets. The DM method is designed for application to a large population of facilities; results are not necessarily applicable for individual facilities or small populations of facilities. Under this methodology, NASA defines acceptable operating conditions in accordance with standards comparable to those used in private industry, including the aerospace industry.

While there have been no significant changes in our deferred maintenance parametric estimating method this year, the analysis of the changes in FCI data between FY05 and FY06 for these assets indicates that across assessment teams, the FCI is consistent and compatible with previous years' DM assessments. Most notably, a slight downward trend in overall FCI is evident, as would be expected due to system degradation over time, while a majority of assets showed no change in FCI. Finally, the majority of the assets whose FCI changed more than three standard deviations can be explained by deterioration and system adjustments-both of which are reasonable explanations for large variations in individual FCI ratings from year to year.

Deferred maintenance related to heritage assets is included in the deferred maintenance for general facilities. Maintenance is not deferred on active assets that require immediate repair to restore them to safe working condition and have an Office of Safety and Mission Assurance Risk Assessment Classification Code 1 (see NASA STD 8719.7).

	2006	Restated 2005
<b>Deferred Maintenance Method</b>		
Facility Condition Index (FCI)	3.6	3.7
Target Facility Condition Index	4.3	4.3
Backing of Maintenance/Repair Est. (Active and Inactive Facilities)	\$2.05 B	\$1.85 B



# Office of Inspector General Letter on Audit of NASA's Financial Statements

National Aeronautics and  
Space Administration

**Office of Inspector General**  
Washington, DC 20546-0001



NOV 9 2006

TO: Administrator  
Chief Financial Officer

FROM: Inspector General

SUBJECT: Audit of the National Aeronautics and Space Administration's  
Fiscal Year 2006 Financial Statements (Report No. IG-07-004)

Under the Chief Financial Officers Act of 1990, NASA's financial statements are to be audited in accordance with generally accepted government auditing standards. The Office of Inspector General selected the independent certified public accounting firm Ernst & Young LLP (E&Y) to audit NASA's financial statements in accordance with *Government Auditing Standards* and Office of Management and Budget's Bulletin No. 06-03, *Audit Requirements for Federal Financial Statements*.

In the *Report of Independent Auditors* (Enclosure 1), E&Y disclaimed an opinion on NASA's financial statements for the fiscal years ended September 30, 2006 and 2005. The disclaimer resulted from NASA's inability to provide E&Y auditable financial statements and sufficient evidence to support the financial statements throughout the fiscal year and at year-end.

The *E&Y Report on Internal Control* (Enclosure 2) includes two reportable conditions, which are considered to be material weaknesses. Material weaknesses were found in NASA's controls for (1) financial systems, analyses, and oversight used to prepare the financial statements, and (2) assuring that property, plant, and equipment and materials are presented fairly in the financial statements.

The *E&Y Report on Compliance with Laws and Regulations* (Enclosure 3) identifies several instances in which NASA's financial management systems did not substantially comply with the requirements of the Federal Financial Management Improvement Act of 1996 (FFMIA). For example, the report notes that certain subsidiary systems, including property, are not integrated with the Core Financial module and are not complemented by sufficient manual preventative and detect type controls. The report also identifies instances of noncompliance with certain provisions of the Antideficiency Act and with the Improper Payments Information Act of 2002.

NASA made significant progress in correcting two of the four deficiencies noted in FY 2005; specifically, Fund Balance with Treasury (FBWT) and estimating environmental liabilities. However, NASA's continued problems in resolving its other internal control weaknesses have contributed to its inability to produce complete and

accurate financial statements. NASA's two remaining internal control deficiencies are material weaknesses that have been reported for several years.

NASA prepared a corrective action plan in FY 2006 to address the material weaknesses and recommendations noted in the FY 2005 financial statement audit report. NASA should address the findings detailed in the enclosed reports and NASA's internally identified material weaknesses noted in the Administrator's Statement of Assurance in a new updated, corrective action plan. That plan must be detailed enough to ensure successful implementation with desired results. In addition, NASA must continue to

- ensure that the Office of the Chief Financial Officer is staffed with properly trained personnel who can address the Agency's financial management and accountability challenges;
- ensure that accounting practices are consistent with applicable standards and are consistently applied;
- establish internal controls that provide reasonable assurance that the financial statements are supported, complete, and accurate; and
- implement recommendations made in E&Y's *Report on Internal Control*, as well as those made by our office and the Government Accountability Office.

E&Y is responsible for each of the enclosed reports and the conclusions expressed therein. Accordingly, we do not express an opinion on NASA's financial statements, internal controls over financial reporting, or compliance with certain laws and regulations, including, but not limited to, FFMIA.

In fulfilling our responsibilities under the Chief Financial Officers Act of 1990, we provided oversight and technical support. We monitored the progress of E&Y's audit, reviewed reports submitted by E&Y, and ensured that E&Y met contractual requirements.



Robert W. Cobb

3 Enclosures

# Report of the Independent Auditors



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## Report of Independent Auditors

To the Administrator and the Office of Inspector General  
of the National Aeronautics and Space Administration

We were engaged to audit the accompanying consolidated balance sheets of the National Aeronautics and Space Administration (NASA) as of September 30, 2006 and 2005, and the related consolidated statements of net cost, changes in net position and financing and combined statements of budgetary resources for the fiscal years then ended. These financial statements are the responsibility of NASA's management.

During fiscal year (FY) 2003, NASA implemented an Integrated Financial Management Program (IFMP) system (now referred to as the Integrated Enterprise Management Program [IEMP] system), specifically the Core Financial Module. NASA's management identified significant errors beginning with its September 30, 2003 financial statements resulting from the implementation of IEMP. During FY 2004 through FY 2006, NASA's management continued to identify and resolve significant system conversion and data integrity issues, implement internal control, and develop policies and procedures. In FY 2005 and FY 2006, internal control and financial reporting processes using the Core Financial Module were continuing to evolve, including the implementation and refinement of routine account analysis and reconciliation processes and the analysis of alternatives in developing effective approaches in accounting for property, plant, and equipment. As a result of these limitations, we were unable to obtain sufficient evidential support for the amounts presented in the consolidated balance sheets as of September 30, 2006 and 2005, and the related consolidated statements of net costs, changes in net position and financing and combined statements of budgetary resources for the fiscal years then ended.

Because of the matters discussed in the preceding paragraph, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the consolidated balance sheets as of September 30, 2006 and 2005, and the related consolidated statements of net cost, statements of changes in net position and financing, and combined statements of budgetary resources for the fiscal years then ended.

In its preparation and analysis of its September 30, 2006 and 2005 financial statements, NASA identified but largely did not quantify certain configuration and data integrity issues and errors in balances reported on its financial statements. The notes to the financial statements describe certain departures from accounting principles generally accepted in the United States of America in NASA's FY 2006 and FY 2005 financial statements. The notes also refer to a potential adjustment for certain mission-related assets (theme assets) that, if recorded, could have a significant impact on the financial statements.

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Report of Independent Auditors  
Page 2 of 2

The information presented in the Management's Discussion and Analysis (MD&A), the Required Supplementary Stewardship Information, and the Required Supplementary Information is not a required part of the NASA's financial statements but is considered supplementary information required by Office of Management and Budget (OMB) Circular A-136, *Financial Reporting Requirements*. Such information has not been subjected to auditing procedures, and accordingly, we express no opinion on it. We were unable to apply to the information certain procedures prescribed by professional standards within the time frames established by OMB because of the limitations on the scope of our audit of the financial statements discussed above. Finally, programs identified in the FY 2005 financial statements do not directly align with the major goals and outputs described in the MD&A.

In accordance with *Government Auditing Standards*, we have also issued our reports dated November 3, 2006 on our consideration of NASA's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and other matters. The purpose of those reports is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. Those reports are an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our work.

*Ernst & Young LLP*

November 3, 2006  
Washington, D.C.

## Report on Internal Control

To the Administrator and the Office of Inspector General  
of the National Aeronautics and Space Administration

We were engaged to audit the financial statements of the National Aeronautics and Space Administration (NASA) as of and for the year ended September 30, 2006, and have issued our report thereon dated November 3, 2006. The report states that because of the matters discussed therein, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the consolidated balance sheet as of September 30, 2006, and the related consolidated statements of net cost, changes in net position and financing and combined statement of budgetary resources for the fiscal year then ended.

In planning and performing our work, we considered NASA's internal control over financial reporting in order to determine our procedures for the purpose of expressing an opinion on the financial statements, which we were ultimately not able to do, and not to provide an opinion on the internal control over financial reporting. We limited our internal control testing to those controls necessary to achieve the objectives described in Office of Management and Budget (OMB) Bulletin No. 06-03, *Audit Requirements for Federal Financial Statements*. We did not test all internal controls relevant to operating objectives as broadly defined by the Federal Managers' Financial Integrity Act of 1982 (FMFIA), such as those controls relevant to ensuring efficient operations. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect NASA's ability to initiate, record, process, and report financial data consistent with the assertions of management in the financial statements. The reportable conditions we noted are described below.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described below, we consider both matters noted—Financial Systems, Analyses, and Oversight; and Enhancements Needed for Controls over Property, Plant, and Equipment and Materials—to be material weaknesses.





## Report on Internal Control

Page 2 of 22

**MATERIAL WEAKNESSES****Financial Systems, Analyses, and Oversight (Modified Repeat Condition)**Overview

In fiscal year (FY) 2002, NASA initiated a seven-year agency-wide effort to provide a single integrated suite of financial, project, contract, and human capital tools to help manage NASA's programs and prepare financial information on a timely basis consistent with evolving OMB guidance. During FY 2003, NASA implemented an Integrated Financial Management Program (IFMP) system (now referred to as the Integrated Enterprise Management Program [IEMP] system), specifically the Core Financial Module. The Core Financial Module replaced ten disparate center-level accounting systems and the NASA Headquarters accounting system, along with approximately 120 ancillary subsystems in operation for the past two decades. This conversion effort necessitated complex, extensive data cleanup, which was not always successfully completed.

Beginning with its September 30, 2003 financial statements NASA's management identified significant errors resulting from the implementation of the IEMP system. From FY 2004 through FY 2006, NASA's management continued to identify and resolve significant system conversion and data integrity issues, implement internal control, and develop policies and procedures. We observed progress in financial management processes in FY 2006, including

- Center Periodic Monitoring Package Submissions—During August 2005, NASA issued a policy requiring each center to perform a monthly process of standardized reviews and reconciliations of financial data to identify anomalies and out of balance scenarios to provide a NASA-wide structure for reconciliation and analysis of financial data. By the 25<sup>th</sup> business day after month-end, the center's Office of the Chief Financial Officer (OCFO) is required to review and certify to the completeness of the package and forward the results to the Headquarters OCFO for further review. All supporting documentation is maintained at each center.
- Fund Balance with Treasury—NASA continued to make progress in resolving its fund balance with Treasury imbalance. Corrective actions continued into the summer of FY 2006 clearing prior reconciling items and resolving current unreconciled balances.
- Implementation of OMB A-123 Process—NASA contracted with an independent accounting firm to assist NASA in its implementation of requirements identified in OMB A-123, *Management's Responsibility for Internal Control* which requires each federal agency to establish, assess, correct, and report on internal control to improve the accountability and effectiveness of Federal programs and operations.

Report on Internal Control  
Page 3 of 22

- Improvement in Processes related to Environmental Liabilities—During FY 2006, NASA implemented updated policies, improved processes, and provided training to the Headquarters and Center technical and financial personnel who prepare the environmental liability estimates.
- Subsidiary Listing of Transactions to Support the General Ledger—Through a coordinated effort between the Competency Center and the Headquarters OCFO, a subsidiary listing of transactions for various real and nominal accounts was provided to support and analyze its general ledger.
- Theme Assets—During August 2006, NASA management met with the Accounting and Auditing Policy Committee (AAPC) of the Federal Accounting Standards Advisory Board (FASAB) to obtain guidance as to whether theme assets, totaling approximately \$12 billion, should be capitalized or expensed as research and development costs. However, a formal decision will not be issued until after November 15, 2006.
- Financial Management System Certification and Accreditation—During FY 2006, NASA had its core financial system certified and accredited.
- Guidance and Training—The Headquarters OCFO has issued updated Financial Management Requirements (FMR) for the remaining five out of 19 chapters and provided additional training to Center and Headquarters personnel.
- Contractor Reported Excess Costs Over Obligations—During FY 2006, as part of its periodic monitoring and year-end closing processes, NASA developed alternative procedures that are expected by management to ensure that excess contractor reported costs and the corresponding obligations would be researched, recorded, and resolved in a timely fashion to ensure appropriate recording of accrued costs and related obligations to its general ledger.

However, significant financial management issues continue to impair NASA's ability to accumulate, analyze, and distribute reliable financial information. Our testing of internal control continued to disclose certain weaknesses, including lack of integrated financial management systems, incomplete efforts to resolve data integrity issues, and weaknesses in entity-wide internal control which impaired NASA's ability to report accurate financial information on a timely basis. In many cases the progress noted above and related processes continued to be developed in FY 2006 and will require additional refinements in FY 2007.

#### Routine Reconciliation, Analyses and Oversight Processes

The U.S. Government Accountability Office's (GAO) *Standards for Internal Control in the Federal Government* states that internal control activities help ensure that management's directives are carried out. The control activities should be effective and efficient in



Report on Internal Control  
Page 4 of 22

accomplishing the organization's control objectives. Examples of control activities include top-level reviews, reviews by management at the functional or activity level, segregation of duties, proper execution of transactions and events, accurate and timely recording of transactions and events, and appropriate documentation of transactions and internal control. During FY 2005, we found that certain processes were not adequately performed to ensure differences were properly identified, researched, and resolved in a timely manner and that account balances were complete and accurate. Although we noted progress during FY 2006, continued emphasis on internal control processes is needed to provide NASA the ability to report accurate financial information in a timely fashion.

Periodic Monitoring Package Submission

At the end of FY 2005, NASA management developed an entity-wide structure for routine reconciliation, analyses, and oversight processes. Throughout FY 2006 and on-going into FY 2007, NASA management continues to identify enhancements to the process. The periodic monitoring package, a monthly process performed at the centers and forwarded to headquarters, is designed to identify issues impacting the integrity of the centers' financial management information and provide a means for communication and tracking of the issues centrally within the Headquarters OCFO. The process includes 23 separate analyses of significant financial processes within the center including, for example, fund balance with Treasury, accounts receivable and payable, budgetary, and contractor reporting. Each analysis is required to include a coversheet depicting the preparer's and reviewer's sign off, whether exceptions exist, and what the exceptions are. The coversheet submissions are due to the Headquarters' OCFO by the 25th business day after the end of each month and require a certification from the center Chief Financial Officer (CFO) indicating their review. Our review of these submissions and the related support maintained at the center identified progress at the centers in identifying issues, including system configuration concerns, continuing data integrity issues—dating back prior to the system conversion in 2003, and other issues requiring immediate attention by NASA management. However, our review of these packages also identified certain weaknesses in processes that could impair NASA's ability to correct material errors in a timely fashion. Specific concerns are as follows:

- Our review of the centers' submissions and the supporting documentation maintained at the centers identified inconsistencies in the procedures performed, the reports utilized, and the results provided among the various centers. Our review of NASA's FMR identified general guidelines as to the reconciliation to be performed, but is not specific as to the reports to be used or the specific procedures to be performed. Per discussions with Headquarters OCFO, additional training, site visits by the Headquarters submission reviewers, and improved guidance are expected during FY 2007.
- During our review of the coversheets and the related supporting documentation, we noted that although the coversheet would indicate no exceptions, the supporting documentation would identify exceptions that were not reported to Headquarters. Additionally, we noted that certain centers did not disclose certain discrepancies because they deemed them as



Report on Internal Control  
Page 5 of 22

agency-level issues and were out of the control of the center. Per center management, formal guidance is needed to explain what is to be identified as an exception on the coversheet.

- We noted certain issues within the centers' submissions that had been identified for several months but had not been resolved in a timely fashion. Per discussions with center management, in most cases, the issues had been forwarded to headquarters either with a service request or the need for headquarters guidance but the center was awaiting guidance. Certain centers indicated that some of the delays occur due to not knowing who to contact at headquarters—primarily due to turnover in headquarters positions. Per discussions with headquarters personnel, as of October 2, 2006, there was a backlog of more than 78 service requests. Headquarters personnel indicated that procedures are still evolving and as a result certain items are still being worked. During FY 2007, headquarters OCFO personnel indicated that they are implementing procedures to resolve many of these items. Currently, other than such service requests, issues identified by the centers are not centrally tracked to determine the extent of the issue.

Fund Balance with Treasury

Treasury regulations require that each federal entity ensure that it reconciles, on a monthly basis, its financial records with Treasury's records and that it promptly resolves differences. If this reconciliation is not adequately performed, loss, fraud, and irregularities could occur and not be promptly detected, and/or financial reports that are inaccurate may be prepared and used in decision-making.

Throughout FY 2003, NASA implemented, in phases, a commercial off-the-shelf, agency-wide, integrated financial management system that replaced ten separate accounting systems in operation at NASA centers. This effort, which involved converting accounting data in the "legacy" accounting systems to a new accounting system, created complex accounting issues for FY 2003. Consequently, as noted in the FY 2003 audit report, as well as in our subsequent audit reports, NASA posted year-end adjustments outside its Core Financial Module, which indicated that the difference between its fund balance with Treasury balance and Treasury's balance was significantly greater than had been presented in its year-end reconciliation. In addition, these adjustments did not provide sufficient documentary evidence to explain the linkage between the adjustments and the unreconciled differences identified on headquarters' fund balance with Treasury reconciliations as of September 30, 2003.

Between FY 2003 and the third quarter of FY 2006, NASA management expended significant effort analyzing its differences related to the conversion and refining its procedures to ensure reconciliations for current activity going forward were performed properly to resolve reconciling differences in a timely fashion. On a monthly basis, these differences are now required to be reported to Headquarters' Office of the Chief Financial Officer via the periodic monitoring submission to ensure appropriate resolution. During June 2006, Headquarters' OCFO in



Report on Internal Control  
Page 6 of 22

conjunction with the centers made the decision to write-off residual pre-conversion differences of \$22 million.

Our review of current year reconciliations identified progress in the preparation and more timely identification and resolution of differences arising from current period transactions. As of June 30, 2006, budget clearing, suspense, and unreconciled differences totaled an absolute value of \$92.6 million. However, although progress was noted, we continued to identify old outstanding items greater than six months old. Additionally, one of NASA headquarters' reconciliation steps to understanding these differences includes identifying differences between amounts in the Central Resources Control System (CRCS) and the Core Financial Module. CRCS is the database used by OCFO for budget control by establishing resource plans for all levels. Each month, Resources Authority Warrants (NF 506) are issued from headquarters to centers and monthly activities are posted to CRCS. NASA personnel indicated differences between CRCS and the Core Financial Module occur because of timing differences on entering funding data and fund allocations in CRCS and the Core Financial Module between headquarters and the centers.

In preparation for the financial management system upgrade—expected to occur in October of FY 2007—NASA management took additional efforts to clear out their suspense, budget clearing, and unreconciled differences during the fourth quarter of FY 2006. At September 30, 2006, we were informed that an absolute value of differences for NASA in such accounts was \$10.7 million.

#### Budgetary Analyses

Within the federal government, the budget is a primary financial planning and control tool. OMB Circular A-11, *Preparation, Submission and Execution of the Budget*, implements the requirements of budget formulation and execution including requirements related to apportionments, accounting systems to control spending, proper recording of obligations, and closing accounts. For internal control purposes, budgetary monitoring is a key management control that, if implemented correctly, identifies cost overruns and potential material misstatements in a timely fashion.

Although we determined that reviews of the budget were being performed at the center and mission directorate level, our review of the budgetary status of funds report identified some negative balances whereby costs appeared to exceed obligations. Additionally, we noted that the centers used different reports to assess funds availability as compared to headquarters. Many of the centers indicated that the negative balances were awaiting correction or the balances in the report could not be relied upon because the amount was based on estimates. The cost over obligations edits (discussed later under “Efforts Needed to Resolve Data Integrity Concerns”), disaggregated estimation process used for certain contract accruals, and CRCS to core financial module process noted above can greatly complicate the review of status of funds reports, and could desensitize reviewers to problems normally inherent in anomalous balances.

Report on Internal Control  
Page 7 of 22

In the past few years, NASA has had more than one possible anti-deficiency act violation. The Office of Inspector General reported there were anti-deficiency violations and management agreed to report as required. To ensure these violations do not continue, enhanced budgetary monitoring processes are required.

Financial Statement Preparation Processes

Our review of NASA's financial statement preparation process identified certain issues impacting NASA's ability to effectively accumulate, assemble, and analyze information to timely develop its financial statements on a routine and recurring basis. Currently, although processes continue to be improved, data integrity issues, systems that are not fully integrated and evolving account reconciliation and periodic analysis processes continue to provide challenges in the development of auditable financial statements. The following represent issues identified during the financial statement preparation process:

- The requirement that each agency submit its Performance and Accountability Report (PAR) by approximately November 15 has created challenges for all agencies. The completed PAR for NASA was not available until the last week of October which did not provide sufficient time to meet deadlines for completion of the audit, review and submission processes. Many agencies have accelerated their PAR process by providing performance and other information as of an earlier date, and holding only very limited sections open for updates of information. Further, for both interim and year-end financial statements, certain analyses were not performed by OCFO until after the financial statements were submitted for audit purposes, suggesting that review processes may not be fully effective. Finally, although we were informed and documentation indicated that the PAR and supporting analyses had been through a rigorous review process prior to our audit, we noted that mistakes and errors were missed by the review process and that much of the preparation and many reviews were performed with contractor assistance. NASA personnel had limited capability to describe how balances reflected in the statements were derived, one aspect of an effective supervision and review process.
- Although NASA had indicated that it performed and upper management had reviewed its quarterly fluctuation analyses of its financial information to identify unusual balances, our review of NASA's analysis of its September 30, 2006 financial statements identified inconsistencies for which we required further explanation. Upon further inquiry, NASA indicated that due to previous data integrity issues, the balances they were comparing created variances that could not be explained. Management expected a better analysis would be available in FY 2007.
- For the third quarter financial statements, NASA had not reconciled all of its intra-governmental balances with its trading partners. Our review of the Treasury difference report identified over \$200 million for which NASA could not identify the reasons for differences with its trading partners. Further, we determined that intra-NASA transactions had not been eliminated from the initial draft of the financial statements.



## Report on Internal Control

Page 8 of 22

Many of these transactions related to services provided to the centers from the new shared service center.

- For both interim and year-end financial statements, we noted that financial statements submitted to OMB and for audit purposes were not compliant with OMB Circular A-136, *Financial Reporting Requirements*. We noted that certain disclosures, including those for net costs, undelivered orders, and intra-governmental balances had not been updated to ensure consistency with new guidance. Checklists and other tools (an annotated copy of A-136) which can help ensure that reports are appropriately prepared were not used effectively to identify the requirements of OMB Circular A-136 to ensure compliance.
- We noted that adequate documentation to support certain transactions was not readily available. Our testing of transactions identified several items where we did not receive sufficient information to determine if the transaction was valid. For example, NASA could not provide documentation to support its assertion that certain accruals were not necessary to be recorded in its financial statements as of September 30, 2006. According to OCFO management, NASA implemented processes intended to minimize the extent of required accruals, and did not record such accruals. We were unable to assess the effectiveness of this process, and whether grantees and contractors accelerated all billings for services rendered through September 30<sup>th</sup> by September 27<sup>th</sup> as the systems were not operating during conversion to the new financial management system. To the extent such processes are not consistent with Federal Acquisition Regulations (FAR) or cost principles associated with execution of grants, it is possible that grantees and contractors would not have advance billed NASA for services that they would normally not draw down funds for or invoice for until late October or November. Depending on the results seen by NASA in the beginning of FY 2007 through a review of subsequent disbursements, it may be possible to modify this approach to incorporate and estimate for any remaining necessary accrual.

### Efforts Needed to Resolve Data Integrity Concerns

NASA's management continues to identify data integrity issues in the Core Financial Module that impairs its ability to prepare accurate and complete financial statements. Data integrity issues identified during FY 2003 and prior continue to impair FY 2006 account balances. Although much progress was seen during FY 2006, our testing continues to identify similar issues. Additionally, although the centers were able to provide subsidiary listings; the listings are frequently being generated from non-routine processes, not directly from the financial management module. Specific concerns noted include the following:

- During FY 2005, we reported that NASA designed its new Core Financial Module to include a system edit whereby, if costs (and the corresponding liabilities) are greater than the associated obligations, the difference would not be recorded in NASA's general ledger but rather maintained outside of the general ledger system. Instead, the differences were adjusted at the contract/project level by posting a liability to match the



Report on Internal Control  
Page 9 of 22

excess costs. Statement of Federal Financial Accounting Standards (SFFAS) No. 1, *Accounting for Selected Assets and Liabilities*, SFFAS No. 4, *Managerial Cost Accounting Concepts & Standards*, and NASA's FMRs require costs to be accrued in the period in which they are incurred and any corresponding liability to be recorded as an account payable. During FY 2006, as part of its periodic monitoring and year-end closing processes, NASA developed alternative procedures that are expected by management to ensure that excess contractor reported costs and the corresponding obligations would be researched, recorded, and resolved in a timely fashion.

As part of its periodic monitoring process, management indicated that the center OCFO is expected to work closely with the appropriate procurement official, the project manager, and the vendor to initiate the necessary contract funding modification actions to record timely increases to obligations, record excess costs, resolve mistakes in vendor reporting, obtain explanations for cost adjustments, and to validate the processes the vendor will have in place to prevent over costing in the future. Once the modification is identified, the center OCFO personnel should record the appropriate transactions to ensure amounts have been reported in the general ledger system. If amounts are not corrected by quarter-end, the center should report the status through its monthly periodic monitoring process to Headquarters' OCFO for assistance.

At year-end, Headquarters' OCFO runs a report that identifies by fund center those "costs over obligation" amounts that have not been resolved nor recorded in the general ledger. Headquarters' OCFO indicated that they then net the balances for each fund center and process top-side entries to the general ledger to either accrue the costs or obligations or process the downward cost adjustment. These entries are expected to be reversed in the first quarter of the following fiscal year so that the centers can perform the appropriate research within the normal quarterly process. It is our understanding that certain accruals of costs and obligations may be against expired funds. Management believes this process is in accordance with federal budgetary requirements.

Due to the timing of the new processes being implemented, we were unable to determine the effectiveness of these processes during FY 2006 to record accruals for costs that were in excess of recorded obligations and related obligations and downward adjustments that were necessary to record such costs in the general ledger at year-end.

- We noted numerous grants and contracts which had periods of performance prior to FY 2006 which had not officially been closed due to limited resources available for follow-up of missing or incomplete documentation from the vendor/grantee and a significant backlog of large amounts awaiting de-obligation. For several years, NASA has utilized an outside contractor to resolve the large backlog. For grants, because of the delay of close-out within the grant system, allocation of current activity costs were being posted as current expense against the expired grant obligation. As of March 31, 2006, we noted over 4,000 grants and 3,000 contracts for FY 2005 and prior which were past their period of performance still awaiting closeout and de-obligation. Further, we noted several grant



Report on Internal Control  
Page 10 of 22

and contract sample items where requested supporting documentation was not available or not part of the official file.

- Although the centers use financial management and ad-hoc reports for management oversight purposes, such as aging analyses and collection initiatives, we noted during our testing that numerous accounts receivable were related to balances that were greater than one year old. Many of the balances relate to current and former employees, vendor amounts, conversion issues, and balances with other government agencies. The number of employee related items and their myriad causes are of note and merit rigorous follow up. As of March 31, 2006, we noted over 16% of accounts receivable or approximately \$28 million greater than one year old. Additionally, we noted inconsistencies among the centers as to the timing of when amounts are posted to the allowance for doubtful accounts.
- Although the periodic monitoring package includes a quarterly step to review unliquidated obligations and accounts payable to ensure balances that are recorded in NASA's financial system are valid and supportable, we noted that the centers do not currently age their undelivered orders or their accounts payable to identify old balances that may require follow-up or de-obligation. As of June 30, 2006, we noted numerous unliquidated obligations and accounts payable that were greater than one year old.
- We noted certain transactions were recorded utilizing budget object classes inconsistent with OMB Circular A-11 guidance. During our testing of grants and contracts, while we noted certain contracts recorded to the grant and subsidy object class, certain contracts were recorded to budget classes consistent with grants.

In some cases, individual items selected for audit testing were further researched and actions were taken by NASA management to follow-up on such items and appropriately resolve them. Similar efforts are needed for numerous other old items.

#### Processes in Estimating NASA's Environmental Liability Require Enhancement

During our review of NASA's unfunded environmental liability (UEL) totaling \$893 million as of September 30, 2006 and related disclosures to the financial statements, we noted that NASA has made progress in resolving several weaknesses that impeded its ability to generate an auditable UEL estimate. Specifically, progress has been made in documenting the UEL process and training the Remedial Project Managers (RPMs) that prepare the estimates. However, NASA has not validated the Integrated Data Evaluation and Analysis Library (IDEAL) software program that it uses to estimate a portion of its UEL estimate. Additionally, while NASA has begun to integrate the OCFO into the UEL estimation process, additional integration is required. Finally, NASA should assess its reporting and disclosure against other similarly situated federal entities and commercial enterprises as an aid in ensuring that disclosures are meaningful.

Report on Internal Control  
Page 11 of 22

IDEAL – The IDEAL software application is a parametric cost-estimating model that estimates the cost of environmental remediation liabilities based on average cost experiences for similar conditions. NASA uses these IDEAL algorithms to estimate approximately \$190 million of its UEL. In addition, IDEAL aggregates and reports on all UEL estimates even if they were prepared externally to IDEAL. As previously identified in our prior reports, the IDEAL model has not undergone an independent software verification and validation. While the inputs to the IDEAL model can be verified, the output of the equations (e.g., the cost estimate) cannot be verified without performing a zero-cost re-estimation of the remediation scenario.

In addition, as the IDEAL data files are part of NASA's support for its UEL estimate, we reviewed the process and noted several other control weaknesses in the application.

- Data Security – The current version of IDEAL is a host/client application. NASA's users enter data into a desktop application that transmits the data to a third-party service contractor. This contractor then processes the data and returns it to NASA over the Internet. During our review we were notified that while the password authentication is secure, all other data transmissions are not.
- SAS 70<sup>1</sup> – NASA's third-party service contractor manages the host IDEAL application and processes the calculation of the UEL estimate. We noted that NASA has not evaluated the controls between itself and its service providers through either a SAS 70 or other mechanism, and did not do so as part of the OMB Circular A-123 process.
- User Defined Interface (UDI) – As noted in prior years, NASA's users have complete access to the parametric equations, cost tables, warning limits and other parameters in the model through the UDI. While a report has been developed that would highlight when the center/facility specific default parameters were modified, it would not identify if any of the global parameters/equations in any of the models were modified.
- Documentation – We noted weaknesses in the printed reports generated by IDEAL as they did not provide a complete record of the information contained in the IDEAL data files. NASA indicated that the electronic data files in IDEAL were the official record for the UEL estimates included in its financial statements. Because IDEAL is a host/client application, NASA does not maintain control over the host application, and therefore, updates and changes made to the host program will alter the processing of NASA's client data since it is recomputed every time it is processed without any archive or electronic audit trail. Electronic IDEAL data files archived by NASA as part of the FY 2006 audit

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<sup>1</sup> A Statement of Auditing Standards No. 70, *Reports on the Processing of Transactions by Service Organizations* (SAS 70) report provides for a service organization's description of its controls that may be relevant to a client's internal control, on whether such controls had been placed in operation as of a specific date, on whether they are suitably designed to achieve specified control objectives, and on whether the controls that were tested were operating with sufficient effectiveness to provide reasonable, but not absolute, assurance that the related control objectives were achieved during the period specified.



Report on Internal Control  
Page 12 of 22

might provide different results when processed by the IDEAL host application in the future.

During our online review of entries within electronic files, we noted that numerous warning and error messages were not addressed in the online documentation as to the cause or reconciliation. For example, IDEAL might provide the user with a warning or error that the limits in a parametric equation were being exceeded. While overriding these warnings might be acceptable, there was typically no documentation to support the override decision.

***OCFO Involvement*** – During FY 2006 NASA made progress in implementing a quality review function that was independent of the centers/facilities that prepared the UEL estimate. It also began to integrate the OCFO into the training of the RPMs and the independent review function. In addition, during our review we noted improvement in the process that the centers/facilities used in preparation of the estimate. However, during our review we noted several accounting matters that might have been rectified earlier with additional center OCFO involvement. For example,

- Year-to-Year Changes - While NASA has begun tracking the technical reasons for changes in the year-to-year UEL estimates we noted weaknesses in tracking and analyzing changes in accordance with the accounting literature.
- Documentation – As part of the new quality review process, the center CFOs statistically sample and review IDEAL documentation. However, it was not always apparent what documentation the OCFO considered during their review. Because of software limitations, certain documentation was not attached in IDEAL as originally planned nor was a note included in IDEAL as to what was considered the official documentation. Finally, we noted discrepancies in the effective dates and versions of estimates in IDEAL.

**Financial Management Systems Not in Substantial Compliance with FFMIA**

The NASA financial management systems are not substantially compliant with the Federal Financial Management Improvement Act (FFMIA) of 1996. FFMIA requires agencies to implement and maintain financial management systems that comply with federal financial management systems requirements. More specifically, FFMIA requires federal agencies to have an integrated financial management system that provides effective and efficient interrelationships between software, hardware, personnel, procedures, controls, and data contained within the systems. The financial management system continues to impair NASA's and the centers' abilities to adequately support and analyze account balances reported.

Although NASA implemented a commercial off-the-shelf financial module approved by the former Joint Financial Management Improvement Program (JFMIP), certain aspects of the NASA accounting system lack integration and do not conform to the requirements. NASA's



Report on Internal Control  
Page 13 of 22

management continues to identify configuration issues in the Core Financial Module that resulted in inappropriate transactional postings. Finally, certain subsidiary systems, including systems used to account for property, plant, and equipment, the largest NASA asset, are not integrated with the Core Financial Module. Specific weaknesses noted include the following:

- Certain subsidiary systems, including all property systems (i.e., NEMS, NRPDB, and CHATS), are not integrated with the Core Financial Module and are not complemented by sufficient manual preventative and detect type controls.
- NASA's management continued to identify certain transactions that are being posted incorrectly due to improper configuration or design within the Core Financial Module. For example, during our review of the centers' periodic monitoring packages, the centers identified abnormal balances within the general ledger. The centers indicated that they believed the differences were caused by the design of the system and that system requests had been forwarded to headquarters for consideration to resolve the various issues. Additionally, during our review of the reconciliation of the financial information (FI) module to the funds management (FM) module, both residing within the IEMP, we noted that discrepancies existed due to journal entries not being properly mapped to both modules when posted.
- Although the amount is not material, the second quarter balance sheet generated from the Core Financial Module did not balance, meaning that assets did not agree to liabilities plus net position. Adjustments were made outside the system to correct this prior to submission of the quarterly statements to OMB.
- The Core Financial Module was still unable to provide a breakdown of costs by the four mission directorates which NASA has identified as significant segments for FY 2005. This is not consistent with the requirements of SFFAS No. 4, which calls for presentation of costs by responsibility segment for each fiscal year presented.
- Due to systematic limitations, NASA centers continue to use alternative approaches to ensure data and financial management information is readily available to make critical decisions. These alternative approaches are inconsistent between centers and may cause varied results in the accuracy of reporting from the centers to headquarters. For example, during our center visits, we noted that some centers use manually created spreadsheets to track invoice due dates to ensure compliance with Prompt Payment Act requirements. However, we noted that other centers rely on IEMP to track the payment due dates for compliance.

We noted that NASA is in the process of implementing a software version update which OCFO believes will address some of the systems implementation issues related to the IEMP.



Report on Internal Control  
Page 14 of 22

Weaknesses in Information Technology General and Application Controls

Several access and segregation of duties issues were noted within the IEMP environment. The level of risk associated with these information technology issues depends in part upon the extent to which financial-related compensating controls (such as reconciliations and data integrity reviews of output) are in place and operating effectively throughout the audit period. Certain controls designed to detect errors or inappropriate processing may also not be executed in a manner which can be expected to identify errors, which, while perhaps not material to the financial statements as a whole, may subject NASA to risks regarding safeguarding of assets. Within the context of the overall weaknesses identified in the control environment referenced in the accompanying comments and although NASA has made progress in addressing and resolving prior year information technology findings, these information technology-related issues along with issues noted by NASA OIG in various engagements and their ongoing review of the SAP Version Update (SVU) project merit continued management focus.

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Due to the severity of these issues, an integrated financial system, a sufficient number of properly trained personnel, well-documented policies and procedures, stronger leadership from the Headquarters' Office of the Chief Financial Officer, and a strong oversight function are needed to ensure that periodic analyses and reconciliations are completed to detect and resolve errors and irregularities in a timely manner.

***Recommendation***

We recommend that NASA continue to develop and refine its financial management systems and processes to improve its accounting, analysis, and oversight of financial management activity. Specifically, we recommend that NASA:

- Continue to strengthen controls related to its entity-wide structure for account reconciliation, analyses and oversight by building consistency among centers, providing more in-depth guidance and training for financial personnel, strengthen headquarters oversight by visiting the centers, periodically requesting the supporting documentation to compare to the coversheets, and to improve communication so that issues may be resolved in a more timely manner.
- Continue to improve its current Fund Balance with Treasury procedures to ensure that all reconciling items are thoroughly researched, properly documented, timely resolved, and reviewed by appropriate center and headquarters OCFO personnel.
- Continue to build on budgetary reviews to ensure that costs incurred are within budget and the potential overruns are identified in a more timely fashion.

Report on Internal Control  
Page 15 of 22

- Continue to improve its financial reporting and internal quality review procedures to reasonably assure that information presented in the Performance and Accountability Report is accurate and is consistent with the requirements of OMB Circular A-136, Financial Reporting Requirements, including rigorous use of checklist and supervisory review processes.
- Ensure that the Core Financial Module has been configured to provide a breakdown of net costs consistent with programs identified in NASA's strategic plan and in the Management's Discussion and Analysis (MD&A) section of the financial statements for both fiscal years presented.
- Continue to enhance its procedures related to confirming intra-governmental balances with its trading partners so that differences identified through the OMB quarterly process do not exist.
- Ensure that systems used to prepare the financial statements are complete and have been sufficiently tested prior to interim and year-end reporting dates. NASA should continue to validate its data within the Core Financial Module to resolve issues with data integrity that date back prior to the system conversion in FY 2003 to ensure that data is accurate and complete.
- Develop reports from the Core Financial Module to facilitate reviews and ensure that agings of transactions and open items, unliquidated obligations, grants, and other key areas are periodically assessed, researched, and resolved. Additionally, NASA should improve its process to more timely close expired travel, grants, and contracts and develop refined guidance on accounts receivable, the allowance for doubtful accounts, and the point when accounts receivable is either referred for collection initiatives or written off.
- Continue to devise short-term and long-term resolutions to systematic and integration issues that complicate use of the IEMP.
- Continue to resolve issues identified in the general and application controls surrounding its financial management systems. Additionally, in light of the financial management system upgrade, we recommend that NASA monitor that its internal control, including periodic reconciliations and analysis, are performed to ensure that further data conversion and other issues do not lead to difficulties in processing transactions and preparing accurate reports in the months and possibly the years to come.
- Continue to focus on filling key vacancies within the financial management organization to enhance overall performance and develop a core team of highly qualified individuals with experience in NASA's financial management processes.



Report on Internal Control  
Page 16 of 22

- Continue to provide training for personnel – at Headquarters and center levels –to ensure that they understand their roles in processing transactions, performing account analyses and reconciliations, maintaining supporting documentation, and updating their knowledge of financial reporting requirements. Additionally, NASA should update guidance to ensure specific guidelines are documented as to the source of data, what comprises an exception/difference, required follow-up with timetables, and documentation retention policies.

Finally, as it relates to the estimation of environmental liabilities, we believe that estimating models and tools such as IDEAL are an accepted practice for improving the standardization of engineering estimates. Therefore, we recommend that if NASA continues to use IDEAL as part of its UEL estimation process, that it: (1) complete the verification and validation of the program; (2) encourage the IDEAL contractor to obtain a Type II SAS 70 from an independent third party service provider to demonstrate the operating effectiveness of its internal controls; (3) improve the security and controls of the application; and (4) develop a process to ensure consistent year-to-year audit trails and documentation.

We recommend continued involvement of the OCFO in the UEL process with specific focus on accounting related matters such as disclosure and documentation. We believe the center OCFO review can be enhanced with the inclusion of accounting related matters in its checklists. The OCFO review checklist should include a review of the determination that IDEAL's parametric data provides the best available estimate or that actual cost data is available that would provide a better estimate. We also recommend that NASA's OCFO continue to self-assess the UEL estimation and aggregation process to identify and correct remaining weaknesses in the UEL process.

**Enhancements Needed for Controls Over Property, Plant, and Equipment and Materials  
(Modified Repeat Condition)**

Consistent with prior year audit reports, our review of property, plant, and equipment (PP&E), totaling approximately \$33.2 billion, identified serious weaknesses in internal control that, if not corrected, could prevent material misstatements from being detected and corrected in a timely manner. As stated in the prior year audit reports, NASA's current process for recognizing and accounting for fixed assets relies primarily on a retrospective review of disbursements to determine amounts which should be capitalized and continues to be heavily dependent on activities at its contractors to recognize any assets created at its contractors. Currently, NASA expenses all costs (except for certain construction of NASA-held real property) and then performs a review of the transactions to determine which costs should be capitalized. The subsequent review and dependence on contractor reporting increases the risk that related costs will not be properly captured and capitalized. Until NASA successfully implements an integrated system for reporting PP&E, and develops a methodology to identify costs that need to be capitalized starting at the budget/procurement cycle through to the processing and disbursing of funds as the transaction is processed, NASA will continue to experience difficulties in recording property-related balances and transactions. During fiscal year 2006, we were informed



Report on Internal Control  
Page 17 of 22

that NASA has completed the first phase of its corrective action plan to flowchart and document the current business processes and procedures for each major category of PP&E. Somewhat simultaneously, NASA identified changes that needed to be made to existing policies Agency-wide and formed a cross-functional team to participate in working groups to re-engineer NASA's current processes and procedures and identify solutions to gaps in the PP&E lifecycle management. Pending implementation and acceptance of new policies and processes by all cross-functional departments within the agency of such overarching solutions, further emphasis on internal and external processes at headquarters, the centers, and the contractor locations is needed to ensure that amounts reported in its financial statements are reliable.

During our FY 2006 testing, we continued to note evidence of significant weaknesses in the property area. The weaknesses we noted during FY 2006, most of which are consistent with last year's audit report, fundamentally flow from not determining at the point of budget formulation, obligation recognition, contract development, accounts payable recognition, or disbursement the amounts of property NASA expects to buy, has contracted for, or has purchased. Rather, NASA waits until the entire transaction cycle is complete to obtain disbursement data for capitalization or, in the case of contractors, expects their contractors to do so. Insufficient internal controls surrounding contractor-held PP&E, NASA-held theme assets, NASA-held work in progress (WIP), and NASA-held real and personal property are addressed below:

Contractor-Held Property, Plant & Equipment

The reliance upon NASA's contractors to report property values at periodic intervals during the year without robust agency-wide detect controls to ensure the reliability and validity of those property values may increase the probability of errors and deficiencies not being detected by NASA or reported by contractors. Throughout the year, the Headquarters OCFO's property branch personnel do perform certain analytical analyses of property balances and transactions reported by NASA's largest contractors that report monthly in Contractor-Held Asset Tracking System (CHATS). This monitoring process, however, currently lacks integration of NASA's procurement and scientific community, with whom contractor accountability primarily resides, and does not include a reconciliation to the costs being incurred by these contractors via the monthly NF 533 reporting process to the property balances reported monthly in CHATS and annually via the NF 1018. Although the OCFO utilizes the Defense Contract Audit Agency (DCAA) as its primary quality assurance mechanism over NASA's contractors, the procedures that DCAA performed on the June 30, 2006 property balances and a sample of fiscal year 2006 transactions cannot alone be relied upon by NASA management to ensure the reliability and validity of contractor-held property values.

***Recommendation***

- We recommend that NASA fundamentally revisit its approach to capitalizing contractor-held property by documenting, analyzing, and implementing robust control changes from end to end, including the involvement of the procurement and scientific community.



Report on Internal Control  
Page 18 of 22

- We continue to recommend that all NASA obligation documents and expenditures be coded to identify whether they relate to a property acquisition to create a record for comparison to recorded property transactions and the CHATS subsidiary ledger. For contractor-held property, this would also include developing a method for reconciling contractor costs incurred via the monthly NF 533 reporting process to those contractor-held property balances reported monthly in CHATS and annually via the NF 1018.

#### NASA-Held Theme Assets Operational and WIP

Beginning in FY 2004 and continuing throughout FY 2006, NASA has undertaken a project to review its policies (both accounting and procedural) with respect to theme assets to identify the specific types of costs that should be capitalized and those that should be expensed.

During fiscal years 2005 and 2006, NASA revisited its process to account for theme assets and developed a number of approaches, most recently positing its current position to the AAPC of the FASAB that nearly \$12 billion of the theme asset activity is fundamentally research and development and that such costs should be expensed. The current position contrasts with earlier views that none or a small part of such activity constituted research and development, and is a significant potential change from prior approaches which led NASA to capitalize billions of dollars in such items. In any case, NASA will face challenges in addressing the question of whether certain land based assets so categorized with the theme assets that travel into space are so unique that the remaining technology and hardware are of no future use and cannot be salvaged or used in other research and development projects (a determining factor in NASA's proposed new approach on assessing whether costs should be capitalized). NASA management hopes to resolve the accounting policy-related aspects of its theme asset accounting independent of potentially longer-term needs to develop appropriate systems to capture such costs (however ultimately categorized). The specific rules for the AAPC to issue authoritative guidance which NASA management could follow in resolving the accounting issue is through a technical release approved by the FASAB, which has not yet occurred.

Management has begun to address the procedural matter, as discussed in previous years' reports, in establishing new policies by incorporating financial and engineering authoritative guidance as well as NASA program/project management policy to ensure consistent application and documentation. As one aspect of addressing the accounting issue over which costs are expensed versus capitalized for theme assets in progress and those yet to be undertaken, management implemented October 1, 2005, the revised the engineering authoritative guidance contained in NASA Procedural Requirement 7120.5C, *NASA Program and Project Management Processes and Requirements*. This requirement defined the four management requirements for formulating, approving, implementing, and evaluating NASA programs and projects and provided for an aligned budget structure and technical work breakdown structure within the Core Financial Module. These initiatives seem to be moving NASA in the right direction for identification of the component parts of theme assets throughout its life cycle. However, it is unclear as of yet how the alignment and the specificity of these pre-established work breakdown structure elements will correlate to the accounting for these costs under the authoritative literature.

Report on Internal Control  
Page 19 of 22

Furthermore, NASA management has not yet demonstrated how these new requirements, when fully operational, will provide sufficient specificity in NASA's purchasing activity to facilitate tracking and reporting of all types of property acquisition activity, including the subset of such activity related to theme assets as projects are initiated and disbursements are made. Prior NASA efforts to obtain and retain documentation to support these assets under its existing policy created challenges.

***Recommendation***

- Once the process of exposing NASA's position relating to the accounting for theme assets to the authoritative standard setters has come to an end, we recommend that management act upon the final technical rulings issued by the AAPC and/or FASAB as promulgated by their charters.
- We continue to recommend that all NASA obligation documents and expenditures be coded to identify whether they relate to a theme asset property-related acquisition to create a record for comparison to recorded property transactions and the work breakdown structure (WBS) of costs incurred that result in capitalized theme assets. This would also include developing a method for reconciling costs incurred via the monthly NF 533 reporting process and recorded by WBS elements in the core financial module related to theme assets under construction (work-in-process) to the amounts reported monthly in CHATS or annually in the NF 1018, as well as the theme asset spreadsheet maintained by headquarters.

**NASA-Held Real and Personal Property**

During our FY 2006 testing, we again noted transactions that were not recorded at the appropriate value based upon the final amount paid to the vendor/contractor (i.e., a "three-way match" between the purchase order, shipping document, and invoice was not performed by NASA personnel), transactions were not recorded in the correct month and/or fiscal year based upon the date of authorized acceptance of the property, the initiation of transactions lacked evidence of written authorization or lacked required supporting evidence (i.e. invoices, contracts), and monthly journal vouchers lacked evidence of a supervisory review. NASA management is reliant upon a monthly evaluation to determine which assets should be capitalized to record these transactions and maintains separate subsidiary ledgers which are not interfaced directly with the Core Financial Module. Management records these property, plant and equipment transactions through a manual journal voucher process, yet there is no formal policy that requires supervisory review and signoff evidencing the approval of these entries prior to their posting in the Core Financial Module. It was noted that during the fiscal year, management recorded approximately \$89 million (net) of adjustments for prior years' property transactions for such items as equipment found during routine inventory processes, components of buildings removed and no longer in use revealed during deferred maintenance reviews, and the discovery of manual input errors on key authorizing documents, such as one for \$133



Report on Internal Control  
Page 20 of 22

million, a result of an extra digit, not found when the transaction was originally recorded. There were also adjustments recorded at the headquarters' level relating to depreciation expense totaling approximately \$24 million. All of these transactions were recorded through the current period operations. The result of these adjustments are further examples of management's need to place additional emphasis on strengthening and enforcing center-related manual prevent and detect controls that extend beyond the finance and logistics departments as these are the baseline controls upon which NASA is reliant. Furthermore, management should revisit their entity-level detect controls at the headquarters level to ensure that monthly reviews of center transactions and differences noted in subsidiary ledger reconciliations are reviewed, resolved, and communicated to center personnel in a timely manner for entry into the Core Financial Module or subsidiary ledgers.

***Recommendation***

We recommend that NASA management:

- Develop more robust center-related manual prevent and detect controls that extend beyond the finance and logistics departments, including a formal policy that requires supervisory review and signoff evidencing the approval of property, plant and equipment entries prior to their posting in the Core Financial Module.
- Revisit their entity-level detect controls at the headquarters level to ensure that differences and corrections are resolved and communicated timely to center personnel for entry into the Core Financial Module or subsidiary ledgers.
- Continue completing its implementation of suggested recommendations and developing detailed corrective action plans. In addition, we once again place further emphasis on recommending that NASA fundamentally revisit its approach to capitalizing property by documenting, analyzing, and implementing robust control changes from end to end to all categories of PP&E. We also recommend that all NASA obligation documents and expenditures be coded to identify whether they relate to a property acquisition to create a record for comparison to recorded property transactions and subsidiary ledgers, be they NASA activities or contractors.



## OTHER MATTERS

### Summary of FY 2005 Material Weaknesses and Reportable Conditions

Issue Area	Summary Control Issue	FY 2006 Status
<b>Material Weaknesses</b>		
Financial Systems, Analyses, and Oversight	Documentation regarding significant accounting events, recording of non-routine transactions, and post-closing adjustments, as well as corrections and other adjustments made in connection with data conversion issues, must be strengthened.  Processes to prepare financial statements need improvement.  Certain weaknesses noted relating to general and application controls.	Modified Repeat Condition.
Further Research Required to Resolve Fund Balance with Treasury Differences	Supporting documentation to support application of rigorous reconciliation processes was not available. Unreconciled differences were identified in the FY 2003-2005 year-end reconciliations.	Progress made; combined with Financial Systems, Analyses, and Oversight Weakness. Corrective actions related to suspense accounts, budget clearing accounts and unreconciled differences are needed.
Enhancements Needed for Controls over Property, Plant, and Equipment and Materials	Controls relating principally to contractor-held PP&E and materials and NASA-held assets in space and WIP need improvement; headquarters oversight needs improvement.	Modified Repeat Condition.
<b>Reportable Condition:</b>		
Internal Controls in Estimating NASA's UEL Require Enhancement	Weaknesses noted in NASA's ability to generate auditable UEL estimates using IDEAL estimating methodology and to identify disclosure items; and enhancing the independent quality review.	Progress made; combined with Financial Systems, Analyses, and Oversight Weakness. Corrective actions related to the IDEAL system and the level of the Office of the CFO participation are needed.

\* \* \* \* \*



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Report on Internal Control  
Page 22 of 22

In addition, with respect to NASA's internal control over Required Supplementary Stewardship Information and performance measures reported in the Management's Discussion and Analysis, we were unable to apply certain procedures prescribed by OMB Bulletin No. 06-03, because of the limitations on the scope of the audit of the financial statements, as discussed in our Report of Independent Auditors, dated November 3, 2006. Further, we did not audit and do not express an opinion on such controls.

We also noted certain other matters involving internal control that we will report to NASA management in a separate letter dated November 3, 2006.

This report is intended solely for the information and use of the management and the OIG of NASA, OMB, and Congress and is not intended to be and should not be used by anyone other than these specified parties.

*Ernst & Young LLP*

November 3, 2006  
Washington, D.C.

## Report on Compliance with Laws and Regulations

To the Administrator and the Office of Inspector General  
of the National Aeronautics and Space Administration

We were engaged to audit the financial statements of the National Aeronautics and Space Administration (NASA) as of and for the year ended September 30, 2006, and have issued our report thereon dated November 3, 2006. The report states that because of the matters discussed therein, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the consolidated balance sheet as of September 30, 2006, and the related consolidated statements of net cost, changes in net position and financing and combined statement of budgetary resources for the fiscal year then ended.

The management of NASA is responsible for complying with laws and regulations applicable to NASA. We performed tests of its compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and certain other laws and regulations specified in Office of Management and Budget (OMB) Bulletin No. 06-03, *Audit Requirements for Federal Financial Statements*, including the requirements referred to in the Federal Financial Management Improvement Act of 1996 (FFMIA). We limited our tests of compliance to these provisions, and we did not test compliance with all laws and regulations applicable to NASA.

The results of our tests disclosed two instances of potential noncompliance with the laws and regulations discussed in the preceding paragraph, exclusive of FFMIA, that are required to be reported under *Government Auditing Standards* or OMB Bulletin No. 06-03. First, NASA's management has determined that it has violated certain provisions of the Anti-Deficiency Act (P.L. 101-508 and OMB Circular A-11). We have been advised that appropriate reporting of the violation was performed during October 2006. Additionally, NASA has potentially violated certain requirements of the Improper Payments Information Act of 2002. During FY 2006, NASA management was unable to provide sufficient documentation to support performance of an annual review of all programs and activities that it administers to identify all such programs and activities that may be susceptible to significant improper payments. NASA management indicated that an assessment was performed to estimate an error rate on research and development contracts related to payments between FY 1997 and FY 2005.



Report on Compliance with Laws and Regulations  
Page 2 of 3

Under FFMIA, we are required to report whether NASA's financial management systems substantially comply with federal financial management systems requirements, applicable federal accounting standards, and the United States Standard General Ledger (SGL) at the transaction level. To meet this requirement, we performed tests of compliance with FFMIA Section 803(a) requirements. However, as noted above, we were unable to complete our audit. Based upon the results of the tests we were able to complete, we noted certain instances, described below, in which NASA's financial management systems did not substantially comply with certain requirements:

- The NASA accounting system does not conform to certain Federal requirements. NASA's management continues to identify data integrity and configuration issues in the Core Financial Module, which results in inappropriate transactional postings. Additionally, certain subsidiary systems, including property, are not integrated with the Core Financial Module and are not complemented by sufficient manual preventative and detect type controls.
- Data within NASA's financial system have not been validated as reliable and may not be reliable to support NASA's financial statements. Additionally, certain data was not readily available to adequately support sufficient reconciliations and analyses of significant fluctuations in account balances, with fluctuation review processes impeded by acknowledged deficiencies in baseline information used in comparisons.
- Reviews of general and application controls over financial management systems identified certain departures from requirements specified in OMB Circular A-127, *Financial Management Systems*, and OMB Circular A-130, *Management of Federal Information Resources*. Additionally, the Office of Inspector General of NASA (OIG) identified certain issues related to systems as part of its Federal Information Security Management Act (FISMA) and other OIG projects.
- As part of its FFMIA self assessment, NASA management has identified its financial management system as a material weakness. NASA management indicated that since the completion of the roll-out of the Integrated Enterprise Managements Program's (IEMP) core financial management system, challenges in system processes, configuration, and capabilities have surfaced. They believe that the current IEMP software system has certain capability limitations which require compensating controls which have not been fully implemented.

The Report on Internal Control and management letter include information related to the financial management systems that were found not to comply with the requirements, relevant facts pertaining to the noncompliance, and our recommendations related to the specific issues presented. It is our understanding that NASA's management agrees with the facts as presented and that relevant comments from NASA's management responsible for addressing the noncompliance are provided as an attachment to this report.

Report on Compliance with Laws and Regulations  
Page 3 of 3

Because we could not complete our audit, we were unable to determine whether there were other instances of noncompliance with laws and regulations that are required to be reported.

Providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit, and accordingly, we do not express such an opinion.

This report is intended solely for the information and use of management and the Office of Inspector General of NASA, OMB, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

*Ernst & Young LLP*

November 3, 2006  
Washington, D.C.

## Chief Financial Officer's Response to the Audit Report of the Independent Auditors

National Aeronautics and  
Space Administration  
**Headquarters**  
Washington, DC 20546-0001



November 8, 2006

Reply to Attn of: The Office of the Chief Financial Officer

TO: Inspector General

FROM: Chief Financial Officer

SUBJECT: Management Response to Audit Report of Independent Auditors

We appreciate the efforts of the Office of Inspector General (OIG), and of the independent auditors under contract to the OIG, to audit NASA's FY 2006 and FY 2005 financial statements. We understand that, due to the continued evolution of NASA's internal controls and financial reporting processes, the independent auditor determined that there was insufficient evidence to support the financial statements. This lack of evidence prevented the auditor from expressing an opinion on the consolidated balance sheets, and the related consolidated statements of net costs, changes in net position and financing, and combined statements of budgetary resources.

The *Report on Internal Control* reflects the progress NASA has made in 2006 by removing Fund Balance with Treasury, a 2005 material weakness, and Estimation of Unfunded Environmental Liabilities, a 2005 reportable condition. The report identified two material weaknesses that continue to be challenges for the Agency: Financial Systems, Analyses, and Oversight; and, Enhancements Needed for Controls over Property, Plant, and Equipment and Materials. NASA will continue to address these remaining issues through NASA's 2007 Financial Audit Corrective Action Plan.

We further appreciate the specific examples of control weaknesses across NASA business areas provided in the auditor's reports. This additional level of specificity, both in general topic area and in specific instance, will be helpful as we move forward in our improvement efforts. This is particularly true in the area of Property, Plant, and Equipment, where we will continue to seek your opinion as we implement the anticipated Accounting and Audit Policy Committee (AAPC) or Federal Accounting Standards Advisory Board (FASAB) guidance for theme asset accounting.

We remain committed to working closely over the coming year with you and your staff as we continue to improve NASA's financial management.

A handwritten signature in black ink, appearing to read "Gwendolyn Sykes".  
Gwendolyn Sykes